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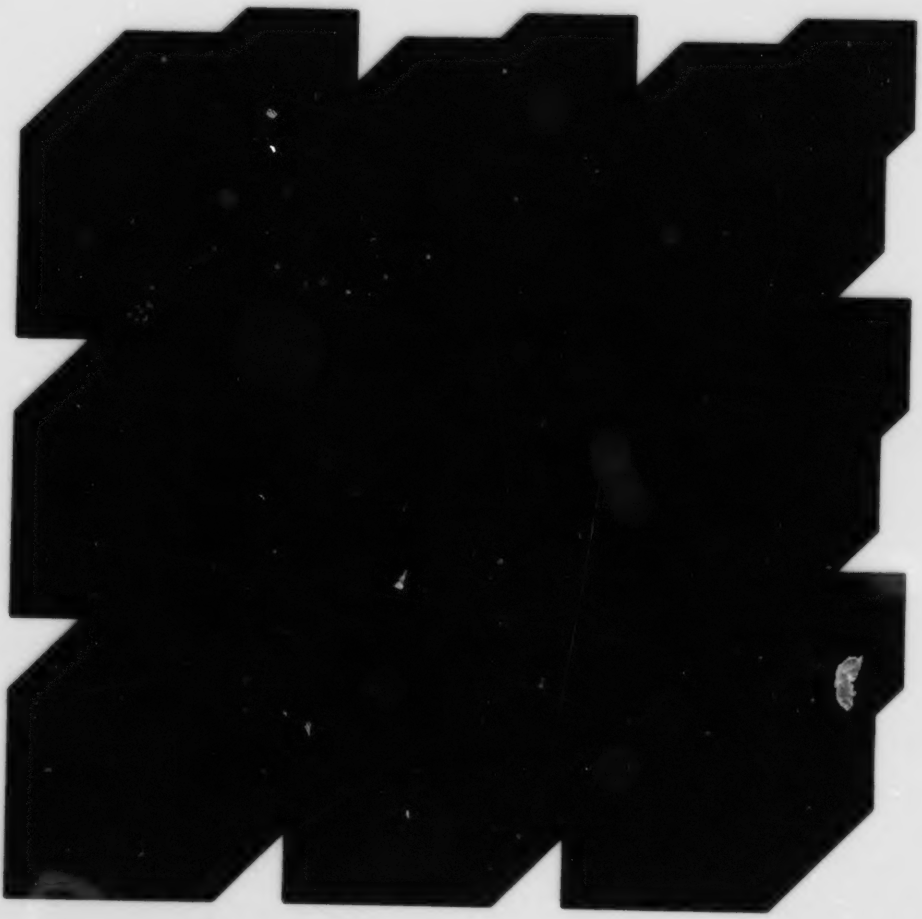

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DISCUSSION PAPER NO. 295

Crown Corporations as Instruments of Public Policy: A Legal and Institutional Perspective

by Elaine Kirsch

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APPENDIX A: Individuals Interviewed

Résumé

L'auteure du présent document énonce d'abord la proposition fondamentale selon laquelle toute entreprise publique canadienne s'accompagne de "coûts" qui découlent directement du contexte juridique et institutionnel où s'exercent ses activités. Si, en respectant la ligne générale de la théorie économique, nous supposons que l'entreprise privée (plutôt que l'entreprise publique) est le meilleur instrument pour maximiser les bénéfices, il s'ensuit que, pour être "acceptables", ces coûts doivent être liés à la réalisation d'un objectif de la politique publique autre que la seule recherche du profit. Dans la mesure où ce n'est pas le cas, ils devraient être éliminés.

Partant de ce principe, elle identifie de nombreux coûts, évidents ou "cachés", des sociétés de la Couronne, qui ne se produiraient pas dans une entreprise privée typique. Elle inclut dans sa définition des "coûts" au sens large certains paramètres, comme ce qu'il faut payer parce que les objectifs de l'organisme sont imprécis, ainsi que les frais qu'entraîne son rôle d'"Agence" selon Jensen et Meckling.

L'auteure présente ensuite les divers objectifs d'une entreprise publique, tels qu'ils sont mentionnés en général dans les écrits sur ce sujet, et constate que peu ou même aucun des coûts examinés ne sont en fait nécessaires à la réalisation des objectifs. En outre - et c'est peut-être là le plus important - l'analyse révèle que probablement aucune entreprise du secteur public n'est, étant donné sa structure, suffisamment motivée pour réduire (et encore moins pour éliminer) ces coûts superflus.

Le dernier chapitre présente l'esquisse d'un modèle qui apporterait à au moins une institution des incitations à tendre vers le but supposément attribué au secteur public, la réalisation des objectifs de la politique publique de la façon la plus efficace par rapport aux coûts. Il ne s'agit pas d'un modèle détaillé. Il est plutôt conçu comme un tremplin pour la création d'une infrastructure favorable à l'intégration de garanties permanentes dans un instrument de politique où toute mesure de la production est pour ainsi dire impossible.

CROWN CORPORATIONS AS INSTRUMENTS OF PUBLIC POLICY: A LEGAL AND INSTITUTIONAL PERSPECTIVE

Abstract

The paper puts forward the following fundamental proposition: there are numerous "Costs" to Canadian public enterprise which derive directly from the legal and institutional environment within which it operates. If we follow the general thrust of economic theory and assume that private (rather than public) enterprise is the most efficient format for maximizing firm profits, it follows that, to be "valid", such Costs must be associated with achievement of some objective of public policy other than pure profit-making. To the extent that this is not so, the Cost should be eliminated.

With this is mind, the paper first identifies numerous Costs -- some obvious, some "hidden" -- of Crown corporations which would not accrue in a representative private sector corporation. The term "Costs" is defined broadly to include parameters such as the cost of imprecise specification of corporate objectives and Jensen-and-Meckling-type "agency costs".

The paper then sets out the various objectives of public enterprise, as generally cited in the literature, and determines that few, if any, of the Costs are indeed necessary to their achievement. Moreover, and perhaps most importantly, the discussion reveals that none of the players in the public enterprise sector likely has adequate structural incentive to reduce (let alone to eliminate) these superfluous Costs.

In its final chapter, the paper sketches a model which would imbue at least one institutional figure with incentives aligned to the assumed public sector goal of achieving public policy objectives in the most cost-efficient manner. The model is not detailed: it is designed, rather, to form a springboard from which to develop an infrastructure which places adequate emphasis on the incorporation of built-in safeguards to a policy instrument for which measurement of output is virtually impossible.

I. Introduction

Recent years have witnessed a proliferation of government studies, commissions and inquiries into the increasingly controversial topic of Canadian Crown corporations.[1] The academic community has equally responded to the challenge of trying to rationalize the Crown enterprise sector,[2] an endeavour which traverses the fields of law, economics, political science and business and involves a "bewildering array"[3] of 650 to 100 federal and provincial bodies, depending on "how you count." As Don Gracey notes:

> Probably no other sector of Canadian public administration has been subjected to such scrutiny over the last decade.[4]

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[1] See, e.g., Canada. Commission to Inquire Into and Report Upon Certain Matters Related to the System of Financial Controls, Accounting Procedures, and Other Matters Relating to Fiscal Management and Control of Air Canada. Air Canada Inquiry Report (Ottawa: Information Canada, 1975) Willard Z. Estey, Commissioner; Canada. Auditor General of Canada. Report of the Auditor General of Canada to the House of Commons for the Fiscal Year Ended March 31, 1976 (Ottawa: Ministry of Supply and Services, 1976) (the "1976 Auditor General's Report); Canada. Privy Council Office. Crown Corporations: Direction, Control, Accountability (Ottawa: Ministry of Supply and Services, 1977) (the "Blue Paper"); Canada. Royal Commission on Financial Management and Accountability: Final Reports, March 1979 (Ottawa: Ministry of Supply and Services, 1979) (the "Lambert Commission Report"); Ontario. The Report of the Royal Commission on Electric Power Planning (Toronto: Royal Commission on Electric Power Planning, 1980) Chairman: Arthur Porter; Saskatchewan. Report of the Crown Investments Review Commission (Regina: Crown Investments Review Commission, 1982) Chairman: W. Wolff (the "Wolff Commission Report")

[2] See, e.g., J.R.S. Prichard, ed., Crown Corporations in Canada (Toronto: Butterworths, 1982); A. Gelinas, ed., Public Enterprise and the Public Interest: Proceedings of an International Seminar (Toronto: The Institute of Public Administration of Canada, 1978).

[3] B.C. Development Corporation et al. v. Karl A. Friedmann, Ombudsman, et al., (unreported decision of the Supreme Court of Canada, November 22, 1984), per Dickson, C.J., as quoted in the Toronto Globe and Mail, November 23, 1984.

[4] D. Gracey, "The Real Issues in the Crown Corportions Debate", in K. Kernaghan, Public Administration in Canada (Toronto: Methuen, 1985), at p. 5.

It is more than likely that such interest will be sustained over the next few years, given the resurgence of Conservative governments throughout the country and the general concern with "privatising" at least part of a sector which accounts for some 10-12% of national G.N.P.[5]

Some of the studies have concentrated on the rationale underlying the choice of public enterprise over other public policy instruments — to use Trebilcock and Prichard's convenient phrase, "the calculus of instrument choice"[6] — or on developing a theory to explain it, drawing largely on the work of the "property rights" school[7] or the "public choice" theorists.[8]

Others have adopted a more factual approach, concluding either that accountability regimes are unsatisfactory and that more control is warranted[9] or that publicly-owned companies are less "efficient" than private enterprise[10], the implicit recommendation being that they be made more profit-oriented.

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[5] Ibid., at p. 1. The most current effort is reflected in the federal government's September, 1984 announcement of its intention to sell off Canadair, de Havilland Aircraft, Teleglobe Canada and Eldorado Nuclear.

[6] M.J. Trebilcock and J.R.S. Prichard, "Crown Corporations: The Theory of Instrument Choice", in Prichard, supra., n.2, at pp. 1-98.

[7] See, e.g., A.A. Alchian, "Some Economics of Property Rights", (1965) 30 Il Politico 816; Alchian and Demsetz, "Production, Information Costs and Economic Organization", (1972) 62 Am. Econ. Rev. 777.

[8] See, e.g., W.A. Niskanen, Bureaucracy and Representative Government (Chicago: Aldine, 1971). Both schools of thought are summarized in T.E. Borcherding, "Towards a Positive Theory of Public Sector Supply Arrangements", in Prichard, supra., n.2.

[9] See, e.g., the Blue Paper, supra., n.1.

[10] See, e.g., D.G. Davies, "The Efficiency of Public versus Private Firms, The Case of Australia's Two Airlines", (1971) 14 J. of Law and Econ., 149 and Crain and Zardkoohi, "A Test of the Property Rights Theory of the Firm: Water Utilities in the United States", (1978) 21 J. Law and Econ., 395, both cited in J. Palmer, J. Quinn and R. Resendes, "A Case Study of Public Enterprise: Gray Coach Lines Ltd.", in Prichard, supra., n.2, at pp.369-446.

Unfortunately, these latter sets of studies involve an inherent dilemma. As suggested in a recent Report to the federal Treasury Board:

> The literature on public administration continues to emphasize the contradiction inherent in government-owned corporations — that is, the need to combine the managerial independence necessary for a corporation operating in the market-place on the one hand with the control and accountability appropriate to an organization using public monies on the other.[11]

That is, much of the "inefficiency" (i.e. divergence from market results) criticized in both the literature and the press derives directly from the fact that, unlike the private sector, Crown corporations must account to "government" — not, as is often implicitly assumed, a single, well-defined entity, but a multi-partite group with manifold incentives. Yet the studies and the media continue to decry the inadequacy of direction, control and accountability in the Crown sector, and legislative efforts (most noticeably in the new amendments to the federal Financial Administration Act ("Bill C-24")[12]) have responded accordingly, only intensifying the dilemma.

The cause of the dilemma is hardly surprising. It results, I would suggest, from the propensity to measure the performance of Crown corporations — particularly the "commercial type" Crown corporations with which we are concerned in this paper — on the same familiar, well-defined basis as we judge other corporations, i.e. profitability, often treated as synonymous with "efficiency".[13] The fact is, and I think few would disagree, that Canadian Crown corporations are rarely created strictly to generate profits[14]; rather, they are established to fulfill other policy objectives such as boosting employment or developing certain regions of the country[15] (we shall refer to these collectively as "Other Policy Objectives"). To quote Trebilcock:

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[11] Canada. Treasury Board. Report Prepared for the President of the Treasury Board (Ottawa: Treasury Board, February, 1984), at p. 60.

[12] 32-33 Eliz. II, 1983-1984, passed by the House of Commons on June 28, 1984 and proclaimed in force on September 1, 1984, amending the Financial Administration Act, R.S.C. 1970, c. F-10.

[13] While this may, indeed, sometimes be accurate in the private sector, it is, at best, a tenuous assumption in the public sector context.

> Using profitability as the measure of performance implies that these enterprises have no objectives other than commercial objectives, but if this was so in many cases it would be difficult to justify the existence of public enterprise.[16]

That is, Crown corporations are simply instruments of public policy (like subsidies, tariffs and tax incentives), clothed in corporate trappings and, consequently, susceptible to being confused with them by people wearing what we shall call "Private Sector Glasses".

I expect that most would share this view. It is, therefore, surprising that few have taken it one step further to say: "True, public enterprise is, generally, not as profitable as public enterprise. But profitability is not, per se, the correct measure of performance[17] — to assume that it is is to wear Private Sector Glasses. Rather, the real issue here is: are the empirically-determined inefficiencies due solely to a loss of allocative efficiency (as is incurred whenever a policy instrument is used to redistribute wealth among members of a society) or to a non-cost efficient (i.e. not productively efficient) means of transferring that wealth? In other words, do the observed differences from private sector performance reflect an efficient formula for achieving Other Policy Objectives? If not, then such differences should be eliminated." It is to this issue that this paper will address itself.

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[14] Note that, in some cases, Canadian Crown corporations have been established for reasons linked to the objective of capturing rents for local residents. The discussion will exclude enterprise created for such purposes.

[15] See discussion infra., chapter 3.

[16] M.J. Trebilcock, Public Enterprises in Papua New Guinea (Papua New Guinea: Institute of National Affairs, 1983).

[17] Except, perhaps, insofar as it affects managerial incentives to monitor; see discussion infra..

We assume, at the outset, that there is some Other Policy Objective(s) which underlies the existence of every Canadian Crown corporation[18] and that such Objective(s) is valid, worthy of being achieved from a political, social or economic point of view. Further, we assume that policy makers have accurately performed the calculus of instrument choice and take the selection of the public enterprise policy instrument as a given.[19] We then put forward the following thesis.

Commercial Crown corporations operate in the same commercial world as do large publicly-owned corporations (like, for example, Bell Canada) but face a significantly different legal and institutional environment. These differences ("Differences") appear in the forms both of potential extra costs incurred by public enterprise in fulfilling a given task ("Costs") and potential privileges ("Advantages") realized by virtue of their close nexus with the Crown. Both translate into potential costs to society, the former by virtue of the fact that society is, ultimately, the "shareholder" who pays for those extra costs (via a higher tax bill) and the latter in the same manner as all subsidies cost society, wearing its hat as taxpayer. These Differences are, therefore, justifiable only if they can be shown to be the minimum necessary to achieve one or more Other Policy Objectives.[20] If this cannot be done, then the Difference should be eliminated and the achievement of Other Policy Objectives should be financially supported by a direct request for funds from government, much in the spirit of the Clark government's Bill C-27, introduced (but never passed) in 1979.

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[18] If no Other Policy Objective exists, then it is arguable that the operation should be privatized. As suggested by Trebilcock and Prichard, "One must assume that to a greater or lesser extent, every Crown corporation is intended to maximize some set of policy objectives in addition to, and indeed in opposition to, profits. If this were not so, it is difficult to conceive of any reason for a Crown corporation to exist." (supra., n.6, at p. 37).

[19] This is not to suggest that I expect that is so performed — indeed, judging by many of the comments made by individuals interviewed, it likely is not. The fact is, however, that whether or not government actually performs the calculus, we live with a huge public enterprise sector: instead of focusing on why we have it, we argue that more emphasis should be placed on attempting to improve it.

Chapters II and III, accordingly, describe in some detail the legal and institutional environment within which Crown corporations at the federal level and in the provinces of British Columbia, Saskatchewan, Ontario, Quebec and to a lesser extent, Nova Scotia[21] operate and, in order to identify the relevant Differences, contrast it with that facing a representative private sector corporation operating pursuant to the Canada Business Corporations Act (the C.B.C.A.).[22] The scope of the chapter is broad and includes parameters not generally associated with the words "costs" — for example, differences in the precision with which corporate objectives are communicated to corporations, in the extent to which information regarding corporate activity is "hidden" from the shareholder, and in the incentives of shareholders, directors and managers to monitor corporate performance. The material is gleaned both from the published literature and from interviews conducted across the country with government officials and senior officers of selected Crown corporations.[23]

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[20] Remember that, by definition, the private sector firm represents the profit-maximizing solution; thus any divergence from private sector costs must relate to Other Policy Objectives.

We emphasize that the Differences are, at this stage in the analysis, merely potential Differences which remain so until actually realized.

[21] These were selected as representing the wide variety of accountability regimes which operate in Canada.

[22] S.C. 1974-75-76, c.33, as amended. The widely-held firm was chosen as many of the Crown corporations under consideration would, if in the private sector, be widely-held (for example, public utilities).

Chapter IV will then list various Other Policy Objectives which Crown corporations might, generally, be expected to achieve. Again, both the current literature and information obtained during interviews have been used as source materials.

Finally, Chapter V will attempt to determine whether or not the Differences highlighted in Chapters II and III represent the minimum input necessary to achieve the Objectives set out in Chapter IV, all the while maintaining our assumption that the calculus of instrument choice duly has been performed.

One note before proceeding. As suggested above there has been, and continues to be, much debate over the appropriate definition of the term "Crown corporation." As stated by Langford and Huffman:

> No such definition exists and the federal government is still a long way from developing an identification and data integration package..."[24]

Definitions range from Langford and Huffman's inclusion of government "corporate enterprises" in eight "functional" categories (but not their subsidiaries)[25], to the definition set out in Bill C-24 which, effectively, includes all wholly-owned corporations and their wholly-owned subsidiaries[26], to the definition suggested by Robert Sexty, virtually abandoning the term "Crown corporation" and replacing it with "government business corporation":

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[23] See Appendix A for a list of individuals interviewed.

[24] J.W. Langford and K.J. Huffman, "The Uncharted Universe of Federal Public Corporations", in Prichard, supra., n.2, at p.221.

[25] Ibid., at pp.288-289.

[26] Supra., n.12, s.95(1).

> ...a legal corporate entity owned or controlled wholly or partially by a government that operates it as an independent business enterprise with the objective of generating sufficient revenues to earn a profit, or at least break even.[27]

Clearly, the development of an appropriate definition could form (and, indeed, has formed) the subject of an entire study and that is not our goal. For our purposes, we adopt the definition chosen by Trebilcock and Prichard and restrict our discussion to "corporations in which the government has a de-facto controlling interest and which, in the words of the [PCO] Blue Paper, provide goods or services directly to the public on a commercial or quasi-commercial basis, i.e. sell their output in a market."[28]

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[27] R.W. Sexty, "Canadian Government Corporations: Definition and Categorization", Working Paper No. 78-7 (School of Business Administration and Commerce, Memorial University of Newfoundland), at p.13.

[28] Supra., n.6, at p. 13.

II. Differences in the Legal Environment

a) Modes of Creation

At the federal level, Crown corporations have been created by either special Act of Parliament, letters patent pursuant to the old Dominion Companies Act or Canada Corporations Act, or Articles of Incorporation pursuant to the C.B.C.A.. Historically, the most prevalent technique has been the first. In recent years, however, "more and more corporations [have been] established by ministers and public servants under companies legislation"[29] without Parliamentary input, fueling the criticism that government has lost control over its public enterprise sector.[30] Likely in response to this, the new amendments to the Financial Administration Act ("Bill C-24") clearly establish the principle that parent Crown corporations can only be created by special Act of Parliament and subsidiary corporations can only be created or acquired with Cabinet approval.[31]

The picture is similar at the provincial level where the bulk of publicly-owned corporations are incorporated pursuant to special Acts of the provincial Legislature (for example, Ontario Hydro[32], Saskatchewan Telecommunications[33] and the Insurance Company of British Columbia("I.C.B.C.")[34]). Here, as well, however, public enterprises can be incorporated or acquired by a Minister without legislative input. In Saskatchewan, this can be done pursuant to Part I, Section 3 of the Crown Corporations Act, 1978[35] (for example, the Potash Corporation of Saskatchewan, subsequently established under its own legislation). In Quebec, the Minister of Transport is authorized to acquire companies for the government and in British Columbia, the Minister of Transportation and Highways can, with the approval of the Lt. Governor in Council, acquire, carry on and operate "any business, commercial or industrial enterprise relating to transport".[36] Cabinet approval must be obtained in all these cases[37]; legislative approval, however, need not. Similarly, in Nova Scotia, several companies have been incorporated under provincial companies legislation without legislative input (e.g. Novaco Ltd.).

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[29] Gracey, supra., n. 4, at p. 2. For example, Ministers can create companies with Governor-in-Council approval under the Atomic Energy Control Act, R.S.C. 1970, c. A-19, s. 10(2).

[30] See, e.g., the Lambert Commission Report, supra., n. 1, at p. 335.

[31] Gracey, supra., n. 4, at p. 6; Bill C-24, s. 101.

[32] The Power Corporation Act, R.S.O. 1980, c. 384.

[33] The Saskatchewan Telecommunications Act, R.S.S. 1979, c. S-34.

[34] The Insurance Corporation Act, R.S.B.C. 1979, c. 201.

The creation of public enterprise by means of special empowering legislation is clearly more costly than preparing and filing Articles of Incorporation, as would our representative private enterprise corporation; it also necessitates resort to the statutory amendment process rather than, simply, to Articles of Amendment if changes ever are to be made to the corporate charter. Further, there is a Cost implicit in the fact that each corporation will be subject to the specific sets of powers, privileges and obligations set out in its constituent Act rather than to the uniform, widely-known standards of a Business Corporations statute.

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[35] R.S.S. 1979, c. C-50.1.

[36] Ministry of Transportation and Highways Act, R.S.B.C. 1979, c. 280, s. 8(b), (c).

[37] Treasury Board Report, supra., n. 11, at p. 57.

On the other hand, if the Crown corporation is created or acquired without input from the legislative body, can Other Policy Objectives properly be communicated and can the public be assured that the calculus of instrument choice properly has been performed?

We will return to this issue in Chapter V.

b) Legal privileges and immunities

In Canada, the Crown itself is clearly entitled to certain legal privileges and immunities. The query thus arises as to whether or not Crown corporations are equally exempted from legal obligations to which private enterprise is subject.

The answer, in general depends not on the extent of Crown ownership *per se* (e.g. 100% vs. 25%) but on whether or not the entity is, in law, deemed to be an agent of the Crown. Accordingly, the first subsection of this section will examine the determinants of Crown agency status and the succeeding subsections will briefly describe immunities in several key areas.

(i) Determinants of Crown Agency Status

Under s. 66(3) of the federal *Financial Administration Act* prior to the Bill C-24 amendments, "Schedule B and C corporations"[38] were expressly defined to be agents of the Crown. Thus, the statute conclusively determined the issue in respect of the 47 companies therein designated.[39]

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[38] Those listed in Schedules B and C to the Act, *supra*. n. 12.

[39] Schedule C included many companies which we would herein call "commercial Crown corporations".

The new Bill takes a different approach to agency status and does not expressly so designate any public enterprise. Rather, s. 95(1) simply defines the term "agent corporation" to mean:

> ...a Crown corporation that is expressly declared by or pursuant to any other Act of Parliament to be an agent of the Crown.

Thus, we must look outside the Act to determine the matter, i.e. to other statutes or to the common law.

Perhaps the most relevant federal Statute in this regard is the Government Companies Operation Act ("G.C.O.A.")[40], Section 3 of which provides that any "Company" to which it applies, "is for all its purposes an agent of her Majesty in right of Canada". Section 2 then defines the word "Company" to mean:

> ...A company incorporated under Part I of the Canada Corporations Act or a corporation incorporated under the Canada Business Corporations Act, all the issued shares of which are owned by or held in trust for Her Majesty in right of Canada except, in the case of a company incorporated under Part I of the Canada Corporations Act, shares necessary to qualify other persons as directors.

Thus, all wholly-owned parent and subsidiary corporations incorporated pursuant to general companies legislation are included within the penumbra of sovereign immunity. For example, in Formea Chemicals Ltd. v. Polymer Corporation Ltd.[41], the Supreme Court of Canada held that in a suit for patent infringement, Polymer Corp. Ltd. (a subsidiary of Polysar) was entitled to the Crown immunity provided for in s. 19 of the Patent Act "by virtue of s. 3(1) of the Government Companies Operations Act". The applicability of the section seemed to be taken for granted and did not merit prolonged discussion by the Court.

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[40] R.S.C. 1970, c. G-7.

[41] [1968] S.C.R. 754.

The G.C.O.A. does not, however, make reference to Crown corporations incorporated by constituent Act and for these we must look to other statutes or the common law.

The first relevant source is the constituent Act itself, many of which declare the enterprise in question to be an agent of Her Majesty in right of Canada: examples include s. 8 of the Teleglobe Canada Act[42] and s. 40(1) of the Broadcasting Act[43] (pertaining to the C.B.C.). These are reinforced in Schedule II to Bill C-24, amending many of the empowering Acts expressly to designate the corporation in question an agent of the Crown.[44] On the other hand, a few statutes specifically negate agency status for the corporations they constitute: examples include s. 13 of the Canada Council Act[45] and s.23 of the Air Canada Act, 1977.[46]

In addition, a federal Crown corporation will automatically be accorded agency status if it was incorporated by a Minister under the Atomic Energy Control Act.[47]

If the constituent Act is silent, we must turn to the common law.

In general, a corporation will not be considered to be the agent of its shareholders, even where the corporation is a corporation sole; this rule was laid down by the House of Lords nearly 100 years ago in the landmark case of Salomon v. Salomon & Co.[48] When, however, the Crown is the shareholder, an agency relationship may nonetheless be held to exist. The relevant test involves a "judicial balancing of the competing aspects of discretionary autonomy and Ministerial control in the constitution and operation of the agency in question"[49], set out by the Supreme Court of Canada in Westeel-Rosco Ltd. v. Board of Governers of South Saskatchewan Hospital Center:

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[42] S.C. 1974-75. c. 77.

[43] R.S.C. 1970, c. B-11.

[44] See list in Appendix B.

[45] R.S.C. 1970, c. C-2.

[46] S.C. 1977-78, c. 5.

[47] Supra., n. 29.

> Whether or not a particular body is an agent of the Crown depends upon the nature and degree of control which the Crown exercises over it. This is made plain in a paragraph in the reasons for judgment of Mr. Justice Laidlaw, speaking on behalf of the Court of Appeal for Ontario in R v. Ontario Labour Relations Board, ex parte Ontario Food Terminal Board, [1963] 2 O.R. 91 at p. 95 where he said:
>
> > It is not possible for me to formulate a comprehensive and accurate test applicable in all cases to determine with certainty whether or not an entity is a Crown Agent. The answer to that question depends in part upon the nature of the functions performed and for whose benefit the service is rendered. It depends in part upon the nature and extent of the powers entrusted to it. It depends mainly upon the nature and degree of control exercisable or retained by the Crown.(emphasis in original)[50]

Thus, at the federal level, most of the Schedule C-II corporations under Bill C-24 and their wholly-owned subsidiaries will be able to take advantage of the privileges and immunities set out below either by virtue of their own incorporating legislation, the G.C.O.A. or the common law.

The situation is slightly more complicated with respect to provincial public enterprise, for, of the provinces canvassed here, only Saskatchewan has created its public corporations pursuant to umbrella legislation, the Crown Corporations Act, 1978,[51] section 5(2) of which states:

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[48] [1897] A.C. 22 (H.L.).

[49] S. L. Goldenberg, "Tort Actions Against the Crown in Ontario", Special Lectures of the Law Society of Upper Canada, 1973 (Toronto: Law Society of Upper Canada, 1973), at p. 381.

[50] [1977] 2 S.C.R. 238, per Ritchie, J., at pp. 249-250.

> A corporation is for all its purposes an agent of Her Majesty in right of Saskatchewan, and its powers under this Act may be exercised only as an agent of Her Majesty.

The constituent Acts of many Crown corporations in other provinces contain express conferrals of agency status; a notable exception is Ontario Hydro which is expressly declared not to be an agent of the Crown for purposes of Ontario's Crown Agency Act.[52]

Unfortunately, numerous constituent Acts remain silent on the issue. In respect of these corporations and those created pursuant to standard companies legislation (where the Crown agency issue is, obviously, not addressed), we must, once again, look to other applicable statutes and the common law.

Perhaps, the most explicit attempt to resolve the problem at the statutory level has occurred in the province of Ontario where The Crown Agency Act[53] states:

> 1. In this Act, Crown Agency means a board, commission, railway, public utility, university, manufactory, company or agency, owned, controlled or operated by Her Majesty in right of Ontario, or by the Government of Ontario, or under the authority of the Legislature or Lieutenant Governor in Council.
>
> 2. A Crown agency is for all its purposes an agent of Her Majesty and its powers may be exercised only as an agent of Her Majesty.

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[51] Supra., n. 35.

[52] R.S.O. 1980, C. 106, s. 3. It has been suggested that the Act was passed specifically to ensure that Ontario public enterprise would have agency status and thereby be immune from federal excise tax; see Colin H. McNairn, "The Ontario Crown Agency Act", (1973) 6 Ottawa L. Rev. 1.

[53] Ibid.

Unlike the G.C.O.A., however, the Courts have not interpreted this statute on its face, but have restricted the meaning of the words "owned" and "operated" so that the operative term of s. 1 has become the word "controlled", effectively the common law test.[54]

In summary, then, at both the federal and provincial levels, agency status (and its important consequences) will be afforded a Crown corporation if expressly conferred by its constituent or another Act or if it satisfies the test in Westeel-Rosco. If the latter route is used, then Costs may be incurred in order to obtain a judicial determination of the agency issue.

One caveat before proceeding. It was suggested by the Supreme Court of Canada in National Harbours Board v. Langelier et al. that a Crown corporation may be an agent for some purposes, but not for others: "It is only when the [corporation] is lawfully executing the powers entrusted to it by the Act that it is deemed to be the Crown agent"[55], the implication being that agency immunities will extend only to certain corporate activity. This approach was recently reaffirmed by the Court and clearly confers agency status where the corporation is "lawfully executing the powers entrusted to it by the Act" (quoting Mr. Justice Martland in Langelier) but not "where...the corporation is not acting for all purposes of [its constituent] Act or with reference to its powers under [its constituent] Act."[56] We do not here pass on the merits of using such a test; for our purposes it is important to note that it suggests that a judicial determination of agency status (and its associated Costs) will be necessary not only in respect of those corporations which are not statutorily admitted to the category, but for all Crown corporations in each context in which they exercise their powers.

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[54] See, e.g., R. v. Ontario Labour Relations Board, ex parte Ontario Food Terminal Board, [1963] 2 O.R. 91, p. 14 (deciding that the Ontario Food Terminal Board is not a Crown agency).

[55] [1969] S.C.R. 60, at p. 72, per Martland, J.

[56] C.B.C. v. The Queen (1983), 145 D.L.R. (3d) 42 (S.C.C.), at p. 51 per Estey, J.

We now turn to the specific privileges and immunities afforded Crown agents.

(ii) Immunity from Statutory Provisions

As a general principle, the Crown in not bound by a statute unless it is expressly named therein or unless it is bound by "necessary implication".[57] This common law rule is now embodied in statutory form in s. 16 of the federal Interpretation Act and in equivalent language in the corresponding provincial Interpretation Acts:

> 16. No enactment is binding on Her Majesty or affects Her Majesty's rights or prerogatives in any manner, except only as therein mentioned or referred to.[58]

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[57] Hornsey Urban District Council v. Hentrell, [1902] 2 K.B. 73; Province of Bombay v. Municipal Corp. of Bombay, [1947] A.C. 58 (P.C.); both followed by the Supreme Court of Canada in C.B.C. v. A.G. Ontario (1959), 16 D.L.R. (2d) 609 (S.C.C.).

[58] R.S.C. 1970, c. I-23; R.S.O. 1980, c. 219, s.11; L.R.Q. 1977, c. I-13, s. 42; R.S.N.S. 1967, c. 151, s. 13; R.S.S. 1978 Cap. I-11, s. 7. Note the reverse presumption in the Interpretation Act, R.S.B.C. 1979, s.14, expressly stating that the Crown is bound unless expressly exempted, except as provided in s. 14(2) thereof. As to the argument that the Crown is no longer bound by "necessary implications", see The Queen in right of the Province of Alberta v. Canadian Transport Commission, [1978] 1 S.C.R. 61.

The presumption of immunity may be invoked not only by the Crown itself, but also by its agents and servants.[59] For example, as the Railway Act[60] nowhere indicates that the Crown or its agents are intended to be bound thereby, it would appear that Teleglobe Canada (expressly declared to be an agent under s. 8 of the Teleglobe Canada Act[61] need not comply with the registration and C.R.T.C. approval requirements stipulated in s. 320 thereof. Similarly, Eldorado Nuclear Limited has, apparently, escaped the application of Ontario environmental protection regulations relating to effluent discharge from one of its refineries[62] and, in 1982, was held, along with Uranium Canada, to be immune from prosecution under the federal Combines Investigation Act[63]. For another example at the provincial level, see Re McGruer & Clark Ltd.[64] where the Ontario Development Corporation was held to be exempt from the requirements of the very important Planning Act.

It would appear that Crown agents are also exempted from prospectus and other disclosure requirements set out in provincial securities legislation. A key case in this regard is Re Caisse de Depot et Placement du Quebec and

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[59] C.B.C. v. A.G. Ontario, supra., n. 57; Regina v. Stradiotto, [1973] 20 R.L. 375 (C.A.); also see Maxwell on the Interpretation of Statutes, 12th ed. (London: Sweet & Maxwell, 1969) at pp. 161-168.

[60] R.S.C. 1970, c. R-2.

[61] Supra., n. 42.

[62] R. v. Eldorado Nuclear Ltd. (1981), 128 D.L.R. (3d) 82 (Div. Ct.).

[63] R. v. Eldorado Nuclear Ltd.; R. v. Uranium Canada Ltd., (1982), 66 C.P.R. (2d) 207 (C.A.).

[64] (1976), 13 O.R. (2d) 385 (Ont. H.C.).

Ontario Securities Commission,[65] where the Ontario High Court held that the Caisse was not subject to the insider trading and take-over bid requirements set out in the Ontario Securities Act. Indeed, the Court went so far as to state that the company (a Quebec Crown agent) was not bound by any of the provisions of that Act, despite the O.S.C.'s convincing arguments that its statutory object of protection of the investing public would be "wholly frustrated" unless the Crown was bound.

If we make the assumption that all legislation is put in place by provincial and federal governments for good reason, then it is clear that immunities such as the ones described in this Section constitute a real Cost to society, be it in terms of pollution (externalities which are not captured), monopoly power, nondisclosure of relevant information regarding the corporation, or any other societal ill which the government, in its wisdom, had attempted to deter.

(iii) Liability in Tort

Early case law held that Crown agencies (as well as the Crown itself) were immune to liability in tort unless the agency's constituent Act expressly reversed the presumption.[66]

This position was set aside some years ago by the Supreme Court of Canada in the Langelier case, Martland, J., stating as follows:

> ...[A] servant of the Crown who commits a wrong is personally liable to the person injured. Furthermore, if the wrongful act is com-

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[65] (1983), 149 D.L.R. (3d)456. Also see D. Gracey, "Crown Corporations: Priveleges and Immunities" (unpublished), Discussion Paper 30/11/83, at p. 4.

[66] Peccin v. Lonegan and T.E.N.O. Ry Comm., [1934] O.R. 701 (C.A.); Formea Chemical Ltd. v. Polymer Corp. Ltd., supra., n. 41.

> mitted by a subordinate at his behest, he is equally liable ....Is the position any different because the agent in this case is not an individual but a corporation? I think not ....
>
> ... In my opinion, if a corporation, in the purported carrying out of its corporate purposes, commits a wrongful act, it is liable therefor and it cannot escape liability by alleging that it is not reponsible for anything done outside its corporate powers -- that is true whether it is purporting to act as a Crown agent or not.[67]

Thus, a Crown agent no longer enjoys an immunity in tort but, rather, may be held liable for wrongful acts or omissions committed either by the corporation *per se* or by corporate subordinates.

Such liability has also been held to exist by virtue of statutory "sue and be sued" clauses. For example, s. 3(3) of the *G.C.O.A.* expressly states that any Company (as defined in s. 2 of that Act)[68] may be sued in its own name and this formula has been held to embrace tort liability.[69] Similar results have obtained at the provincial level.[70]

There remains one possible legal argument for insulating a Crown agent from tort liability. In *Wellbridge Holdings* v. *Winnipeg*,[71] it was suggested by the Supreme Court of Canada that the Crown would not be liable for tortious acts committed in the course of a legislative or quasi-judicial function, but might be subject to liability for a tort committed in the exercise of administrative, ministerial or business powers. Similarly, in *Anns* v. *London*

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[67] *Supra.*, n. 55, at p. 72; see also *P.P.F. Loc. 488* v. *C.B.C.* (1979), 97 D.L.R. (3d) 56 (T.D.).

[68] *Supra.*, text accompanying n. 40.

[69] *Smith* v. *C.B.C.*, [1953] 1 D.L.R. 510; see also Goldenberg, *supra.*, n. 49, at p. 375.

[70] See, e.g., *McGrane* v. *B.C. Ferry Authority* (1968), 1 D.L.R. (3d) 562 (B.C.).

[71] [1970] 22 D.L.R. (3d), 470 (S.C.C.).

Borough of Merton,[72] the House of Lords drew a distinction between policy-oriented or "discretionary" acts, for which no liability would ensue, and "the practical execution of policy decisions" or decisions in the "operational area." It does not appear that either of these cases has yet been argued in defending a Crown agent from tort liability. For example, in Patrick L. Roberts Ltd. v. Sollinger Industries Ltd[73], the Ontario Development Corporation was held liable for negligently giving advice as to whether or not the defendant would receive financing; no reference was made to Anns or Wellbridge Holdings.

For purposes of this paper, we therefore assume that liability will ensue, as with any private corporation and that no Advantage accrues in this area.

(iv) Liability in Contract

At the federal level, section 3(3) of the G.C.O.A.[74] establishes that Companies coming within that Act can be sued directly for any breach of promise made on behalf of the Crown:

> 3.(3) Actions suits, or other legal proceedings in respect of any right or obligation acquired or incurred by a Company on behalf of Her Majesty, whether in its name or in the name of Her Majesty, may be brought or taken by or against the Company in the name of the Company in any court that would have jurisdiction if the Company were not an agent of Her Majesty.

Given the explicit power to contract afforded these Companies in s. 3(2) of the Act, there would not appear to be any bar to directly contractual liability.[75]

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[72] [1977] 2 All E.R. 492 (H.L.), at p. 500

[73] (1978), 3 B.L.R. 174 (Ont. C.A.).

[74] Supra., n. 40.

In addition to this provision, many of the Acts constituting Canadian Crown corporations contain "sue and be sued" clauses, for example, s. 8 of the Teleglobe Canada Act.[76] These have been interpreted liberally by the courts, if anything, generally erring in favour of an aggrieved plaintiff.[77]

If the Crown corporation in question fits neither of these categories, a plaintiff may still bring suit under the common law doctrine of "warranty of authority", levying personal liability under a contract for an agent (here, the corporation) which has, without actual authority, expressly or impliedly represented to a third party that it can bind the principal, if the third party relied on that representation in entering into the contract.[78]

Thus, in summary, Crown agents will usually be liable in contract and no Advantage exists here.

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[75] As always, the plaintiff may well face a more practical problem. viz. that the corporate agent has no assets upon which to realize a judgment and that the Crown itself must be joined as a defendant.

[76] Supra., n. 42.

[77] See, e.g., Langlois v. Canadian Commercial Corp., [1950] S.C.R. 954; Yeats v. C.M.H.C., [1950] S.C.R. 513.

[78] P.W. Hogg, Liability of the Crown (Melbourne: The Law Book Company Ltd., 1971), at pp. 140-141. Note that in Dunn v. MacDonald, [1897] 1 Q.B. 555 (C.A.), the English Court of Appeal held that a Crown servant could not be held personally liable for such cause of action. However, Canadian authorities suggest that this decision is explicable on its facts, has been followed only in Ireland and has no application for Canadian Crown corporations. See Hogg, ibid., G. Williams, Crown Proceedings (1948), at p. 3, and Street, Government Liability (1953), at p. 93.

(v) Liability to pay Income Tax

As a general rule, the Crown is entitled to an immunity from tax. This results from two distinct principles of law:

(a) the imposition of taxes must necessarily have a statutory basis; and

(b) the Crown and its agents are immune from the provisions of any statute unless expressly named therein: this includes the federal Income Tax Act ("I.T.A.").[79]

Thus, we turn to the relevant taxing statutes and their provisions concerning Crown agencies.

Before so doing, in order to keep the discussion well-ordered despite the morass of applicable income tax provisions, the reader should remember that there are four relevant situations to deal with: federal taxes paid by federal Crowns, provincial taxes paid by federal Crowns, federal taxes paid by provincial Crowns, and provincial taxes paid by provincial Crowns.

Two further points should be noted before specific provisions are examined. Firstly, the provisions of the I.T.A. regulate both federal and provincial taxes for the eight "Agreeing Provinces", i.e. those which do not collect taxes directly but allow Ottawa to do it for them and then collect from Ottawa. This means that only Quebec and Ontario (the two Non-Agreeing Provinces) will have taxation statutes relevant to our discussion. As well, British Columbia has its own provisions regulating corporate capital tax, and these will have to be examined.

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[79] R.S.C. 1970, c. I-5, as amended. See Re C.B.C. Assessment, [1938] 4 D.L.R. 764 (Ont. C.A.) and C. McNairn, Governmental and Intergovernmental Immunity in Australia and Canada (Toronto; University of Toronto Press, 1977), at pp. 126,128.

Secondly, in 1977, the federal government and all provinces but Saskatchewan and Alberta established the principle in a "Federal-Provincial Reciprocal Taxation Agreement" that all federal Crown corporations would pay provincial taxes and all provincial Crowns would pay federal taxes in the same manner as would a private enterprise corporation, subject to specific legislation to the contrary.[80]

Down to some specifics. S. 149(1)(d) of the I.T.A. expressly exempts from tax:

> ...a corporation, commission or association not less that 90% of the shares or capital of which was owned by Her Majesty in right of Canada or a province ... or a wholly-owned subsidiary to such a corporation, commission or association...

The Department will permit this exemption to extend to wholly-owned subsidiaries of wholly-owned subsidiaries of Crown corporations[81] although this is merely an administrative practice which need not be upheld in a court of Law. Thus, it would, at first, appear that all Crown corporations under discussion here are immune to federal income tax, whether or not they are agents of Her Majesty.

The picture is not quite that simple, however, for s. 27 of the Act negates the s. 149(1)(d) immunity for the corporations listed in the Income Tax Regulations and expressly declares them to be subject to income tax.[82] These include most of the federal Crown corporations under discussion here. Hence, these will be subject to federal income tax and provincial tax in the eight Agreeing Provinces.

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[80] Gracey, supra., n. 65, at p. 2. I have been advised that there may be a federal-provincial agreement subsequent to 1977 which may include Alberta and Saskatchewan but have unable to locate it. In any case, corporations such as Air Canada which are not exempted from paying federal income tax pay tax in these two provinces, both Agreeing Provinces.

[81] Interpretation Bulletin IT-347R, September 20, 1982, paragraph 8.

[82] SOR/DORS 1984-1048. Before Bill C-24, s. 27 exempted all Schedule D corporations under the old Financial Administration Act.

The provincial Crowns are also exempt from paying federal income tax under s. 149(1)(d) of the I.T.A.[83] and s. 27 does not reverse this immunity. It remains, therefore, only to examine the status of the federal Crowns with respect to Ontario, Quebec and B.C. corporate tax, and the status of the provincial Crowns with respect to provincial taxes.

In Ontario, sections 49 and 63(1) of the Corporations Tax Act[84] create exemptions for Crown corporations from tax on income and on paid-up capital. Section 12(10), however, constitutes the provincial analogue to the federal s. 27 in that it denies the tax exemption to those corporations specifically designated in section 401 of the Regulations under the Act: these include our commercial-type Crown corporations (e.g. Air Canada, CNR Company and Polysar Limited).[85]

The province of Quebec is equally unwilling to provide exemptions for federal Crown corporations. While s. 985 of the Taxation Act[86] states that:

> A corporation, commission or association, the shares, capital or property of which are at least 90 per cent owned by Her Majesty in right of Canada or a province ... is exempt from tax...,

s. 192 of the Act expressly supercedes it to tax any corporation, "carrying on a business as an agent of Her Majesty or of the Government, unless otherwise provided by the regulations" (emphasis added).

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[83] In this context, we include Saskatchewan, as the afore-mentioned Federal-Provincial Agreement only applied to federal corporations' payment of provincial tax.

[84] R.S.O. 1980, c. 97, as amended.

[85] R.R.O. 1980, Reg. 191, as amended by O. Reg. 254/82 and O. Reg. 756/83.

[86] Loi Sur les Impots, L.R.Q. 1977, c. I-3, as amended.

The scheme would, at first, appear to reverse the s. 985 exemption for all agent corporations. The regulations, however, then perform a "double reversal":

> For purposes of s. 192 of the Act, s. 985 applies to every Quebec and Canadian Crown corporation with the exception of the following corporations:... Air Canada ... C.N.R. ... C.B.C. ... PetroCanada ...[87]

The net result is, therefore, effectively the same as at the federal level: federal, commercial-type Crown corporations pay tax in Quebec.

Finally, the B.C. Corporation Capital Tax Act[88] subjects certain Crown corporations to capital tax in that province. The relevant provision is s. 20 which exempts all corporations falling within s. 149(1) of the federal Income Tax Act but then goes on to designate by regulation the Crown corporations which may not take advantage of the statutory immunity. These are listed in B.C. Reg. 489/76[89] and include, essentially the same companies as are taxed in Ontario and Quebec.

Thus, for all intents and purposes, the federal Crown corporations with which we are here concerned pay both federal and provincial taxes throughout the country (except in Saskatchewan and Alberta).

In contrast, provincial public enterprise pays virtually none.

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[87] R.R.Q. (1981), c. 3 1-3, r. 1, a. 192 R1. Translated from the French: "Aux fins du premier alinea du l'article 192 de la loi, l'article 985 de cette loi s'applique a toutes corporations de la Couronne ou du Canada a l'exception des corporations suivantes: ...".

[88] R.S.B.C. 1979, c. 69.

[89] Materials to update this Regulation were not available while doing research.

We have already seen the exemptions provided for under s. 149(1)(d) of the federal Income Tax Act, sections 49(1) and 63(1) of Ontario's Corporations Tax Act, s. 985 of Quebec's Taxation Act and s. 20 of the B.C. Corporation Capital Tax Act. Analogous exemptions exist in the other jurisdictions under study. This represents a distinct Advantage over private sector competitors (as the latter often point out) and a large Cost to the provincial taxpayers who are financing this subsidy.[90]

As to land and property taxes, s. 125 of the Constitution Act, 1867[91] exempts the Crown from taxation with respect to its "lands and property"; this privilege appears to extend to provincial and federal Crown agents.[92] However, in recognition of the services (water, sewers, etc.) provided by the municipalities in which they reside, most Crown corporations, nonetheless, pay "grants" to such municipalities either directly or through the Minister of Public Works.

(vi) Criminal Liability

As a general rule, the Crown and its agents are not subject to criminal prosecution. Thus, for example, in C.B.C. v. A.G. Ontario,[93] the Canadian Broadcasting Corporation could not be prosecuted for broadcasting on Sunday, contrary to the provisions of the Lord's Day Act. In the course of its judgment, the Supreme Court of Canada paid heed to the corporation's statutory mandate to carry on a national broadcasting service within Canada and interpreted this to envisage broadcasting "unlimited as to times".[94] To apply the prohibition of the Lord's Day Act against the C.B.C. would, therefore, have been unduly to interfere with the powers that it exercised as an agent of Her Majesty.

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[90] Note that when I put this issue to one corporate officer, he claimed that his company (one of the country's largest) would not, in any case, pay tax as all income would be eaten up in capital depreciation.

[91] 30 Vict., c.3 as amended by the Canada Act, 1982, 30 & 31 Eliz. II, c.11 (assented to March 29, 1982), formerly The British North America Act.

[92] Supra., n. 65, at p. 3.

[93] Supra., n. 57.

This immunity is not, however, universal, recent Courts having tended to draw a distinction between the Crown and its agents for purposes of criminal liability. Thus, in R. v. Canadian Broadcasting Corporation et al.,[95] the Ontario Court of Appeal held that the C.B.C. was not immune from prosecution under s. 159(1)(a) of the Criminal Code for broadcast of an obscene firm. Brooke, J.A., speaking for the Court, said at p. 246:

> Only if I am satisfied that the Corporation is really the Crown and not merely an agent of the Crown should there be immunity in these circumstances. The statute declares it to be an agent and while the notion of a Crown corporation with its special controls and inability to pay a fine unless it is free to use Crown money may distinguish it from a private person or corporation for some purposes, it is not sufficient to lift it beyond that of an agent. (emphasis added)

The decision was affirmed on appeal to the Supreme Court of Canada.[96]

It is uncertain, at this stage, exactly which test will govern. Certain cases suggest that it is whether the application of the penal provision in question would adversely affect the performance of a Crown function or, to put it another way, would frustrate Crown business.[97] Colin McNairn proposes that the better test would be to "look to the powers conferred upon the entity to see if a breach of the criminal statute was a natural consequence of their proper execution."[98] Unfortunately, the Supreme Court sidestepped the matter in the C.B.C. case, expressly declining to comment upon the majority and minority decisions in C.B.C. v. A.G. Ontario,[99] referring to the Stradiotto test,[100] but then, effectively, approving the lower Court's decision on the ground that the C.B.C. was "exercis[ing] its powers in a manner inconsistent with the purposes of the [Broadcasting] Act, [thereby] step[ing] outside its agency role".[101] That is, in broadcasting the allegedly obscene film, the C.B.C. was not acting as a Crown agent and the issue of when agency immunity would pervail was rendered moot.[102]

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[94] Ibid., at pp. 618 and 621.

[95] (1980), 30 O.R. (2d) 239.

[96] Supra., n. 56.

[97] See, e.g., R. v. Berriman (1883). 4 O.R. 282 (H.C.J.); R. v. Stradiotto, supra., n. 59.

Whatever test ultimately emerges, there is little doubt that agent corporations will realize some Advantage (and society will recognize a corresponding Cost) associated with their immunity from criminal prosecution.

(vii) Labour Relations

There is no uniform system governing employer-employee relations in Crown corporations--some follow the specific procedures set out in special government employee legislation (the Public Service Employment Act[103] and the Public Service Staff Relations Act[104] at the federal level, and statutes such as Ontario's Crown Employees Collective Bargaining Act, 1972 ("C.E.C.B.A.")[105] at the provincial level) and others follow the legislation pertaining to the private sector (e.g. the federal Canada Labour Code[106]).

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[98] Supra., n. 53, at p. 125.

[99] Supra., n. 56, at p. 50.

[100] Ibid., at p. 52.

[101] Ibid., at p. 53.

[102] It is most interesting that the Court implicitly assumed that the film involved was obscene (and hence outside the intent of the Broadcasting Act, such that the C.B.C. was not acting as an agent) in order to determine that the C.B.C. could be prosecuted to determine whether or not the material was obscene.

A full discussion of which corporations fall into which group is beyond the scope of this paper. Suffice it to say that, in general, the commercial-type corporations under study here follow the same legislative dictates as does private enterprise, the notable exception being Ontario which includes all employees of Crown agents in the definition of "Crown employees"[107], subject to the provisions of the C.E.C.B.A.[108] They are, thus, except for persons "employed in a managerial or confidential capacity"[109], *inter alia*, prohibited from striking (s. 27), a clear Advantage for the Crown corporation involved and a subsidy from one subset of society (the Crown employees) to the corporation. On the other hand, the Act imposes certain restrictions on the corporation as employer (e.g. ss. 10, 27 and 29); further, it is generally agreed that wages for "Crown employees" are higher than for employees of comparable private companies. Thus, Costs are also incurred by the Ontario public enterprise, likely more than offsetting the above-noted Advantage.[110]

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[103] R.S.C. 1970, c. P-32.

[104] R.S.C. 1970, c. P-35.

[105] R.S.O. 1980, c. 108.

[106] R.S.C. 1970, c. L-1.

[107] *The Public Service Act*, R.S.O. 1980, c. 418, s. 1(1)(e); exception is made for Ontario Hydro (not in any case a Crown agent) and the Ontario Northland Transportation Commission. See, in general, K. McCarter, "The Legal Environment of Crown Corporations in Ontario" (unpublished manuscript) (Toronto: University of Toronto, Faculty of Law, 1978), at p. 42.

[108] *Supra.*, n. 105.

[109] *Ibid.*, s. 1(1)(1).

There are several other Differences which exist in the labour relations area, stemming largely from government's tendency to include Crown corporations in omnibus legislation relating to the public sector. Thus, for example, in British Columbia, employees of "public sector employers" (including any corporation whose board has a majority of its members appointed by an Act, a Minister or the Lieutenant Governor in Council) are subject to the provisions of the Compensation Stabilization Act,[111] the purpose of which is to "encourage productivity and restrain and stabilize compensation in the public sector."[112] Similarly, federal Crown corporations were subject to the government's recent "Six-and-five" program, are subject to the Official Languages Act,[113] and will now be subject to the "Employment Equity" program, just announced by the new Conservative government and designed to equalize employment opportunities for women, native Canadians, minorities and the disabled.[114]

Another, more subtle, Cost is that associated with the fact, identified by senior corporate officers across the country, that their employees tend to keep one eye on the remuneration and benefits received by other Crown sector employees. While it is true that private sector employees likely also cite collective bargaining precedents, the problem is, apparently, exacerbated in the public sector arena.

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[110] A review of comparative wage structures in the public and private sectors is beyond the scope of this paper, as is a balancing of the noted Advantage and Costs.

[111] S.B.C. 1982, c. 32, ss. 1, 2.

[112] The Compensation Stabilization Amendment Act, S.B.C. 1983, c. 13, s. 2.1.

[113] R.S.C. 1970, c. O-2.

[114] Toronto Star, March 9, 1985. Note that federally-regulated companies are also to be subject to the program.

It is difficult to determine the magnitude of these assorted Costs. For purposes of this study, we assume that they are small but not negligible.[115]

(viii) Priorities as a Lender

In Canada, the Crown is given certain special priorities in the commercial law area. A key example is found in section 107(1)(j) of the federal Bankruptcy Act[116] which entitles the Crown to rank as a preferred creditor (i.e. after secured lenders but before the unsecured) in bankruptcy proceedings. Crown agents are equally entitled to this privilege,[117] and, hence, yet another Advantage -- i.e. subsidy to Crown corporations -- is recognized.

The priority does not, however, extend to all aspects of commercial law. Thus, in Re Mar Lise Industries Ltd.,[118] McDermott, J. did not permit the Industrial Development Bank ("I.D.B.")[119] to take advantage of the Crown's privilege to maintain a priority position when it failed to renew a registration pursuant to the Ontario Bills of Sale and Chattel Mortgages Act. Rather, he drew a distinction between the Crown and its agents for this purpose:

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[115] The exception is when legislation like the Compensation Stabilization Act freezes salaries of management, as would likely not happen in the private sector. Such Costs (in terms of attracting and holding good managers) are non-negligible and will be addressed infra. in subsection (i) of Chapter III.

[116] R.S.C. 1970, c. B-3.

[117] Re Spartan Services Ltd., [1960] O.W.N. 431; Re Goodwyn (1983), 48 C.B.R. (N.S.) 14; Re Selinor Inc. (unreported, Quebec Superior Court); Re Forte (1984), 46 O.R. (2d) 199 (Ont. S.C.).

[118] C.B.R. (N.S.) loc. cit., at p. 151.

[119] Predecessor of the Federal Business Development Bank.

> I do not think that s. 26 [creating the Crown privilege] is intended to apply to a mere agency of the Crown...If it does apply to such an agency, then I think the whole purpose of the registration provisions of the Act would be defeated.[120] (emphasis added)

The decision was affirmed by the Ontario Court of Appeal which felt it unnecessary to rule on the applicability of s. 26 to the I.D.B. and affirmed on other grounds.[121]

If the reasoning of McDermott, J. prevails on future appeals, it would presumably extend to a failure to register or renew a security interest under a provincial Personal Property Security Act or equivalent statute and the Advantage suggested by the Bankruptcy Act and case law thereunder would therefore be limited. It does, however, exist, and represent a subsidy to Crown corporations from the unsecured creditors who would collect in a bankruptcy proceeding but for s. 107(1)(j); as such, it must be justified by an Other Policy Objective.

(ix) Disclosure

Under s. 41 of the Federal Court Act,[122] a Minister may request that a document of a Crown agent be withheld from production and discovery if the public interest in withholding such document outweighs the "public interest in the proper administration of justice". The determination is made by the Court.

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[120] Supra., n. 118, at p. 152.

[121] 5 D.L.R. (3d) 487.

[122] R.S.C. 1970, chap. 10 (2nd Supp).

It is difficult to determine how often (if at all) this privilege is claimed in the context of our commercial-type Crown corporations. If and when it is, it represents an Advantage to the corporation and a subsidy by the other parties litigant to the suit in question.

It is also an interesting exemption to note in light of the fact that many of the commercial Crown corporations are subject to the federal Access to Information Act[123] (and equivalent provincial legislation). Such disclosure represents a Cost to public enterprise which is not incurred in the private sector and which will be particularly disadvantageous to Crown corporations which operate in competitive markets if they thereby have to disclose otherwise highly-confidential materials.

(x) Procedural Privileges

Crown agents are often the beneficiaries of special limitation periods or notice provisions. For example, in Ontario, section 11 of the Public Authorities Protection Act effectively narrows the limitation period for bringing action for breach of statutory or other public duty or authority to six months whereas Ontario's Limitations Act would generally permit two years in which to bring an action for "penalty, damages...given by any statute...."[124] The scope of this protection has been limited by the Supreme Court of Canada to those "aspects of the statutory powers and duties [of the Crown agency] which have a public aspect or connotation and does not comprehend ... planning, construction and managerial responsibilities which have a private executive or private administrative application or are subordinate in nature"[125], but the Act still confers a distinct Advantage.

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[123] S.C. 1980-81-82-83, Chap. 111, Sch. I.

[124] Public Authorities Protection Act R.S.O. 1980, c. 406. Limitations Act, R.S.O. 1980, c. 240, s. 45(1)(h). See also McCarter, supra., n. 107, at pp. 36-41.

In addition, certain empowering statutes specifically provide for beneficial limitation periods for the corporations which they create. For example, s. 31(1) of Ontario's Power Corporation Act[126] limits the time within which a plaintiff may bring an action against Ontario Hydro under sections 24-27 thereof (regarding frequency changeover) to one year.

Similarly, certain Advantages obtain in that special notice provisions are provided for in some constituent Acts. For example, s. 31(2) of the Power Corporation Act provides that no s. 24-27 claim may be brought against Ontario Hydro unless the complainant has served notice of same upon the company within 90 days of the date upon which the cause of action arose.[127]

Such Advantages all represent subsidies from potential plaintiffs to Crown corporations.

(xi) Remedies

It has been held in both Ontario and Saskatchewan that Crown agents are not subject to injunctive relief, provided they are acting within the scope of their statutory authority,[128] a test reminiscent of the Supreme Court's approach in the area of criminal liability.[129]

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[125] Berardinelli v. Ontario Housing Corporation (1978), 90 D.L.R. (3d) 481 (S.C.C.) at p. 495, per Estey, J.

[126] Supra., n. 32.

[127] Note, however, that agent corporations cannot, apparently, take advantage of the 60 day notice requirement set out in Ontario's Proceedings Against the Crown Act, R.S.O. 1980, c. 393: Jessome v. Ontario Housing Corporation (1981), 31 O.R. (2d) 305.

Such immunity creates yet another important Advantage for Crown corporations and a corresponding subsidy by a distinct subset of the Canadian public (successful plaintiffs for whom a remedy limited to damages may not be adequate).

(xii) The Canadian Charter of Rights and Freedoms[130]

The effect of this very new and stimulating branch of Canadian constitutional law on Crown corporations could easily occupy a chapter of its own. For present purposes, we would simply note that to the extent that the American requirement of "state action" is incorporated into emerging Canadian legal doctrine, and to the extent that agent corporations are considered to be "state actors", they may have to comply with Charter provisions from which private sector competitors would be exempt. If so, then a direct Cost will be recognized.

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[128] Banner Investments Ltd. v. Saskatchewan Telecommunications (1977), 78 D.L.R. (3d) 127; Saskatchewan v. Royal Bank, [1982] 1 W.W.R. 60 (Sask. Q.B.); Kohler Drugstore Ltd. et al. v. Ontario Lottery Corp et al. (1984), 46 O.R. (2d) 333.

[129] Supra., text accompanying n. 95.

[130] Supra., n. 91, Part I.

III. Differences in the Institutional Environment

a) Monitoring Costs

There are several sets of costs which are often subsumed under the rubric of "monitoring costs", those associated with determining whether or not firm goals have been achieved. For example, Coase refers to reducing the "costs of negotiating" a separate contract for each aspect of production as one factor influencing the emergence of firms in the economy.[130] To the same end, McManus looks to the "costs of enforcing" performance under such individuallynegotiated contracts in the face of the promisee's propensity to "chisel" or "shirk".[131] Trebilcock postulates that the high "transactions costs" of ensuring that private beneficiaries of government subsidies don't "cheat" favour the use of public enterprise as a policy instrument.[132] Alchian and Demsetz construct a model centered on an owner who acts as a "specialized monitor," with strong incentive, as the residual beneficiary of the firm's product, to keep monitoring costs to a minimum.[133] One might equally refer to "information costs", "specification costs", or, in the context of public enterprise, "accountability" -- the nomenclature is different in each case, but all stress the importance of the costs of monitoring achievement of the firm's wealth-maximizing objectives.

This section of this chapter -- and it is a lengthy one -- will focus on the intricate systems of monitoring performance in Crown enterprise which have developed in the jurisdictions under study in contrast to that which has evolved in the private sector. It is divided into three subsections:

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[130] R. Coase, "The Nature of the Firm" (1937), 4 Economica 386.

[131] McManus, "The Costs of Alternative Economic Organizations" (1975), 8 Can. J. Econ., 334.

[132] Trebilcock, supra., n. 16, at p. 26.

[133] Alchian and Demsetz, supra., n. 7.

i) Who acts as monitor and what incentives exist to ensure that he monitors well?

ii) How does the monitor do his job, i.e. what institutional monitoring/accountability/reporting mechanisms are used?

iii) Perhaps most importantly, how well are corporate objectives communicated to and understood by the various monitors?

i) The Monitors

The private sector corporation has three potential monitors -- the shareholders, the directors and firm management. In practice, all are involved in monitoring achievement of the firm's (profit-maximizing) goal. The shareholders elect directors (C.B.C.A., s. 101(3)), appoint auditors (C.B.C.A., s. 127), and if necessary, fire the directors and elect new ones. The directors, in turn, appoint and fire the officers (C.B.C.A., s. 116) and generally, "manage the business and affairs of the corporation" without shareholder intervention, except to the extent required by corporate Articles, by-laws or a unanimous shareholder agreement (C.B.C.A., s. 97(1)). They also review the auditor's statement, approve financial statements, and prepare the Annual Report (C.B.C.A., s. 149(1)). Management conducts day-to-day operations and exercises those powers which the board has delegated to them.[134] Thus, all three tiers of corporate actors are involved in monitoring corporate performance.

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[134] All may be delegated except for those set out in s. 110(3) of the C.B.C.A., such as declaring dividends, approving a takeover bid circular and approving the company's financial statements.

How well do they do so in practice? The literature would suggest that it is quite well, largely because the incentive structure facing each is conducive to efficient and effective monitoring.

The property rights theorists, perhaps best exemplified by Alchian and Demsetz,[135] emphasize the relative ease with which property rights (i.e. ownership units in firms) can be exchanged or transferred. This has two important consequences in the context of the shareholder's incentive to monitor. Firstly, as residual beneficiary of the firm's wealth, she will have a direct stake in promoting corporate wealth in the cheapest manner possible. Secondly, if we assume that there is a relatively efficient market for the firm's shares and that the price of those shares reflects the present value of the firm's wealth/future stream of profits, then the shareholder has a well-defined, easily accessible, objective measure of firm performance. This not only reduces the absolute cost of monitoring (relevant to "how" she monitors, in subsection (ii)), but should actually increase her propensity to monitor, because it makes monitoring easy: if share prices drop significantly, there is little doubt that shareholders will demand an explanation from management.

Ease of asset transferability also has a direct effect on managers'[136] incentives to maximize profits, as there is an abundance of instruments directly tied to share price -- including profit-sharing plans, stock options, and the threat of mergers or takeovers -- which exist to help bring their goals into line with those of the shareholders. This is crucial in motivating good managerial performance and in keeping monitoring costs low, for, as Williamson,[137] Jensen and Meckling[138], and others have pointed out, the manager's primary motivation is not to increase firm wealth, but to maximize his own welfare, as dictated by his personal Utility function. This in turn, is dependent on both pecuniary and non-pecuniary variables[139]: to the extent that these coincide with the shareholders' desire to maximize firm wealth and to the extent that managers can be made to internalize the cost of non-pecuniary consumption, agency costs[140] and monitoring costs will be reduced.[141] All the more so to the extent that the "rental rate" for the manager's human capital (surely a variable in his Utility function) will increase in proportion to profits made by the firm[142]: his reputation is on the line, and it is largely determined by profit levels.

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[135] Supra., n. 7.

[136] Following the literature, we treat directors and managers as essentially synonymous for purposes of the analysis.

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[137] As cited in Alchian, "The Basis of some Recent Advances in the Theory of Management of the Firm" (1965), Journal of Industrial Economics, 30.

[138] Jensen and Meckling, "Theory of The Firm: Managerial Benavior, Agency Costs and Ownership Structure" (1976), 3 Journal of Financial Economics, 305. See also, E. Fama, "Agency Problems and the Theory of the Firm" (1980), 88 Journal of Political Economy 288, where the implicit assumption of a single owner/manager is relaxed.

[139] A more extensive discussion of the non-pecuniary variables, as suggested by Niskanen and others, will follow infra..

[140] Agency costs are equal to the divergence between the results of the manager/"agent's" decision and the profit-maximizing decision. See Jensen and Meckling, supra., n. 138.

[141] Note that agency costs will never likely be reduced to zero, but only to the point where the marginal cost of monitoring equals the marginal wealth increment from reduced consumption of perquisites by managers. See Jensen and Mecklin, supra., n. 138.

[142] See Fama, supra., n. 138, at p. 58.

Incentives aside, directors and managers are probably quite good at what they do as they have likely been chosen on the basis of their expertise, either in the firm's product market or as "professional managers".[143]

Thus, all the shareholders, directors and managers of our benchmark representative private corporation likely have the incentives and skills appropriate to relatively efficient monitoring of their company's performance.

How does the Crown corporation match up against this benchmark? Again, we have shareholders, directors and managers available as potential monitors: do they operate in the same manner and with the same incentives and expertise as in the private sector?

The answer, as might be anticipated is, unfortunately, no, and we examine the three roles one by one to determine where Differences exist.

1) The Shareholders

Although, de jure, the shares of Crown corporations are generally held by a Minister in trust for the government, it would be a grave error to thereby assume that this is the individual whose role should be compared to the private sector shareholder. Rather, the surrogate "shareholder" of public enterprise comprises many different entities and varies across the jurisdictions under study here.

The first level of what we shall call "layering" appears in the very question of who the Crown corporation is ultimately responsible to -- Parliament (or the provincial Legislature) or the government of the day, in the guise of the Minister who holds the share(s). In practice, it tends to be the latter[144] even where, in law, it is the former.[145] The very uncertainty will generate some Costs in the form of specification of respective duties, duplication of effort and incentives to monitor.

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[143] See, e.g., A. Chandler, The Visible Hand (1977).

The next, and more severe level of layering occurs in the practice of, either de jure or de facto, requiring the involvement of a wide array of government entities to perform the various monitoring functions, such as approving capital budgets, approving borrowing, approving corporate plans and similar documents, appointing directors, etc. As such schemes vary significantly across the jurisdictions, we will describe each individually.

At the federal level, approval of Crown corporations' capital budgets (considered by many interviewed to form the primary check on corporate performance) must be obtained from the Minister of Finance (if borrowing is involved), the President of the Treasury Board and the "appropriate Minister" (who holds the share(s)), as well as the Cabinet (Bill c-24, s.131)[146], four separate tiers of endorsement.

The appointment and removal of directors lies technically within the domain of the responsible Minister but, in practice, requires extensive consultation with regional Ministers and caucus leaders[147] and the approval of the Governor-in-Council (Bill C-24, s.114(1)); their remuneration, however, is controlled by Cabinet, on the advice of the Advisory Committee on Senior

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[144] Gracey, supra., n. 4, at p. 13.

[145] See, e.g., Bill C-24, s. 98.1.

[146] Gracey, supra., n.4, at p. 7.

[147] Ibid.

Executive Compensation (the secretariat of which is provided by the Privy Council Office).[148]

Corporate plans must be submitted to the appropriate Minister, Cabinet, and if required under the Regulations, the Minister of Finance (Bill C-24, s. 129(1)). Summaries of the plan follow a slightly different route, going first to the Minister and then to Parliament and any Committee which Parliament thinks appropriate (Bill C-24, s. 132(3), (4)). Surprisingly, the format of these documents must conform to any Regulation made in its regard by the Treasury Board (Bill C-24, s. 133).

The corporate auditor is chosen, as would be expected, on the approval of the Minister and the Governor-in-Council. While, as we shall soon see, most auditors are external, there is yet another government monitor involved here, and that it is the Auditor General (an officer of Parliament), a figure who has taken a most active, visible and controversial role in monitoring federal Crown corporation performance.[149]

Finally, since August 1983, yet another monitor — the Associate Secretary of the Treasury Board — has been charged with "supervision of the Crown corporations policy area" and a new "Crown Corporations Directorate" consisting of 53 people has been established "to minimize duplication of efforts ... and clarify procedures for ... Crown corporations ...".[150] The Associate Secretary position is apparently vacant as of the time of writing, but, presumably, will soon be filled; it constitutes yet another level in the shareholder hierarchy.

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[148] Ibid.

[149] See, e.g., Report of the Auditor General of Canada to the House of Commons for the Fiscal Year Ended March 31, 1976, supra., n. 1, Chapter 5; Canada. Auditor General of Canada. Report of the Auditor of Canada to the House of Commons for the Fiscal Year Ended March 31, 1979 (Ottawa: Ministry of Supply and Services, 1979), Chapter 8; Canada. Auditor General of Canada. Report of the Auditor General of Canada to the House of Commons for the Fiscal Year Ended March 31, 1982 (Ottawa: Ministry of Supply abnd Services, 1982), Chapter 2.

Several of the above points will be recanvassed, infra, in the context of how monitoring is accomplished (subsection (ii). They are mentioned here, however, to illustrate the panoply of federal entities which, at various times and for varying purposes, assumes the role of shareholder of federal Schedule C-II Crown corporations: the appropriate Minister, the Minister of Finance, the President of the Treasury Board,[151] the Cabinet, the Legislature, the Auditor General, the Associate Secretary of the Treasury Board, and assorted Parliamentary Committees. Of course, each of these "actors," really encompasses numerous civil servants in the guise of "staff"; I was advised that since Bill C-24 has come into operation, the staff of the Crown corporation branch of Treasury Board has been increased nearly three-fold.

The Differences from the private sector are distinct and will be summarized after we review the shareholder hierarchies in the other jurisdictions under study.

In Ontario, accountability for Crown corporations is also officially vested in a "responsible Minister" who reports to the provincial Legislature. In fact, however, as at the federal level, there are numerous layers of monitors involved in the process.

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[150] Government of Canada News Release (May 11, 1984). See also Gracey, supra., n. 4, at p. 5.

[151] Unlike in Saskatchewan, it is highly unlikely that one individual will hold all three of these posts.

The scheme of budget approval which applies for each Crown corporation depends on the terms of the Memorandum of Understanding[152] which that corporation has entered into. Generally, Schedule II corporations are required to submit both operating and capital budgets to the Minister for approval,[153] but if funds from the Consolidated Revenue Fund are required, Management Board and Cabinet will also be involved.

The Memorandum itself is subject to a relatively costly series of approvals, as it must be reviewed and approved by the responsible Minister, Management Board[154] and the Cabinet itself, before being tabled in the Legislature,[155] four tiers of scrutiny on top of the corporate board of directors and management.

The borrowing power of Ontario Crowns is also generally set out in the Memorandum of Understanding. As in the case of Ontario Hydro, Cabinet approval must usually be obtained in addition to that of the responsible Minister, and the corporation may further have to consult with the Minister of Treasury and Economics.[156] In fact, Rule 25, s. 2(h) of the Ontario Manual of Administration makes specific reference to the applicability of the Manual of the Office of the Treasury to corporate borrowing authority.

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[152] The form and content of these will be discussed further, infra. All Schedule II corporations must enter into one of these pursuant to Rule 25 of the Ontario Manual of Administration.

[153] For example, Ontario Hydro and the Ontario Lottery Corporation.

[154] Rule 25, Ontario Manual of Administration, p. 25-2-2.

[155] R.D. Carman, "Accountability of Agencies" (paper presented to the Standing Committee on Public Accounts) (Toronto: Management Board Secretariat, 1983), at p. 2.

[156] Internal working papers supplied by the Economic Council of Canada.

Several other government monitors are involved in corporate activity. For example, the authority of Ontario Hydro to set rates is officially vested in its Board, much as it would be in a private corporation. However, the corporation must then "consult" with the Minister of Energy (its responsible Minister) and, further, must submit all changes in bulk electric rates to the Ontario Energy Board (the "O.E.B.") which acts in an "advisory" capacity. It is not clear how much liaison occurs between these two government representatives (the Minister and the O.E.B.); on at least one occasion, rates approved by the O.E.B. have been changed following complaints from certain rate payers and a written direction from the Minister.[157]

The O.E.B. has on occasion gone further in its inquiries. For example, in 1974, it inquired into Ontario Hydro's expansion programs and financing (much as might the Minister, the Cabinet or the Public Accounts Committee of the Legislature, *infra*.). Similarly, in 1979, it inquired into the "principles governing electricity costing and pricing", again much as might any of the other monitors of the company's cross-subsidization pricing policies.[158]

Ontario Hydro estimates that its annual cost of appearing before the O.E.B. lies in the vicinity of $1.0-1.5 million.

In addition to the use of Memoranda of Understanding, Ontario has made a unique contribution to public enterprise monitoring in the form of regular Sunset Reviews of certain corporations.[159] The Review involves many public players: the responsible minister, the appropriate Policy Field Committee

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[157] *Ibid.*

[158] *Ibid.*

[159] These are discussed in more detail, *infra.*.

Board, Cabinet and the Legislature. Consultation may also occur with other ministries, individuals, and groups "as necessary."[160]

There are two Committees of the Ontario Legislature which may also be involved from time to time in monitoring corporate performance. The first, the Public Accounts Committee, receives the report of the Provincial Auditor and may examine any issues raised therein; during 1983, it called to account five Schedule II corporations and their responsible Ministers[161] as well as Mr. R. D. Carman, Secretary of the Management Board of Cabinet. One of the results of that latter appearance was the Committee's request for Gillian Gillespie's paper, referred to elsewhere in this study.[162] In 1984, the Committee examined recent construction and repair programs at nuclear generating stations and the write-off of several major installations, much as might the responsible Ministry, the O.E.B. or the Cabinet.

The Procedural Affairs Committee (a standing Committee of the Legislature) may also become involved within its mandate of reviewing the government's overall management and control of agencies and corporations; that is, it is in effect a monitor of the other monitors.

This summary has identified at least eight governmental entities (in addition to the Legislature) involved in monitoring Crown corporation performance in Ontario: the responsible Minister, the Cabinet, Management Board, the Minister of Treasury and Economics, the Ontario Energy Board, the Public

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[160] Treasury Board Report, supra., n. 11, at p. 34.

[161] Ibid., at p. 40.

[162] G.M. Gillespie, "Crown Corporations in Selected Canadian Provinces" (Report for the Standing Committee on Public Accounts) (Toronto: Management Board Secretariat, 1984).

Accounts Committee, the Procedural Affairs Committee and various Policy Field Committees.

A similar situation prevails in British Columbia where a Cabinet minister is designated but other entities play leading monitoring roles.

The Cabinet here is most active, appointing directors and officers and setting their remuneration (unless the corporation's empowering statute states otherwise[163]), approving major capital projects and appointing the auditor (unless the constituent Act specifies the Auditor General[164] or gives the Minister of Finance such power[165]). This last function, however, requires the recommendation of the Chairman of the Treasury Board and is subject to the terms of reference proposed by the Treasury Board and the Office of the Comptroller General.[166]

Despite the activities of all these parties, it is generally agreed that primary financial control[167] in British Columbia is exercised not by the Cabinet but by the Minister of Finance as fiscal agent pursuant to Fiscal Agency Agreements entered into with most Crown corporations.[168] On the other hand, regular financial reporting is done through the designated Minister (who, for example, receives reports of the Auditor General). Thus, monitoring of financial performance is vested in three separate entities: the Cabinet, the Ministry of Finance and the responsible Minister.

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[163] For example, B.C. Rail and the British Columbia Development Corporation.

[164] For example, Expo '86.

[165] For example, B.C. Place Limited.

[166] Treasury Board Report, supra., n. 11, at p. 9.

[167] Which, as we shall see in subsection (ii), tends to be the primary monitoring technique.

[168] Discussed further infra..

Probably the most unique feature of monitoring in British Columbia is the role played by the provincial Legislature and its Committees. In 1977, the Crown Corporations Reporting Act[169] was passed, establishing the Committee on Crown Corporations with mandate to "generally inquire into and examine the management, administration and operation of [the British Columbia Ferry Corporation, the British Columbia Hydro and Power Authority, the British Columbia Railway Company, the Insurance Corporation of British Columbia and the Housing Corporation of British Columbia[170]]" (s. 2(1)).

The Committee was composed of 15 members[171] (Government and Opposition but no Cabinet members) and employed staff of approximately three to ten employees who were not civil servants. Subcommittees were formed (they numbered five by fiscal 1982) and the entire Committee met approximately once a month. Day-to-day contact was maintained between the corporations and the Committee staff who reviewed operation, planning and financial/management reports. The Committee spent $348,936.00 in its fiscal year ended March 31, 1982 and estimated an expenditure of $415,000.00 for its uncompleted fiscal year ending March 31, 1983.[172]

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[169] R.S.B.C. 1979. c. 84.

[170] The last of which is no longer active.

[171] British Columbia. Legislative Assembly. Fourth Annual Review of Operations (Victoria: Committee on Crown Corporations, 1982). At last count, the membership appeared to include 12 individuals, 7 from government and 5 from the Opposition.

[172] Ibid.

The Committee has not been called since the fall of 1983 and the Crown Corporation Reporting Repeal Act[173] may soon be passed by the re-instated Social Credit government to disband it, presumably in pursuance of that government's movement towards fiscal restraint. The Committee has, however, generated some degree of interest across the country as a potential "single window" monitor.

Other relevant government monitors in British Columbia include the Public Accounts Committee which receives the Auditor General's Annual Report (including Consolidated Statements for the "commercial" Crown corporations) and has the right to question the corporations thereon, and the Auditor General herself, who, pursuant to sections of the Auditor General's Act[174] is eligible to be appointed auditor of a Crown corporation and, if not so appointed, is entitled to access corporate records and to "reaudit" any company which she considers worthy of attention.

Finally, we have other involved Committees and Ministers such as the Continuing Committee on Traffic Safety[175] which monitors I.C.B.C.'s achievement of the (traffic safety) Other Policy Objective and the Minister of Industry and Small Business which helps assess applications to the British Columbia Development Corporation ("B.C.D.C.") of over $1,000,000.00.

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[173] First Session, Thirty-Third Parliament, 32 Eliz. II, 1983 (Bill 21), Legislative Assembly of British Columbia. As to the effectiveness of the Committee, see discussion infra., text accompanying n. 259.

[174] R.S.B.C. 1979, c.24, ss. 16, 17.

[175] Composed of the Attorney General, the Minister of Highways and Transport, the Minister of Consumer and Corporate Affairs and the Manager of Traffic Safety of the Insurance Company of British Columbia ("I.C.B.C.").

In summary, the situation in British Columbia mirrors that in the federal jurisdiction and Ontario in that it involves a wide variety of government monitors: the Cabinet, the designated Minister, the Minister of Finance, to a lesser extent, Treasury Board, and various Committees (including, for six years, one very active Committee). They sometimes overlap in functional responsibility, sometimes require several levels of approval where one might suffice and often assume monitoring responsibilities which would belong to a board of directors rather than shareholders outside the public sector.

The province of Saskatchewan emphasizes less the ministerial role and more the function of its unique monitoring entity: a public holding company, originally called the Government Finance Office, then the Crown Investments Corporation ("C.I.C.") and, since the election of Premier Devine in 1982, the Crown Management Board ("C.M.B")[176]. Its mandate includes approval of corporate capital budgets and strategic plans, appointment and setting remuneration of senior management, advising and assisting Crowns in areas such as accounting, legal matters and research, and, generally, communicating government policy to the corporations under its jurisdiction (the "commercialtype" Crowns). It represents a concerted effort to create a single government monitor of corporate performance and, as such, merits some extra attention on our part.

The C.M.B. is composed of eight Ministers (including the Premier who, according to one individual interviewed, rarely attends meetings) and three non-Ministers all appointed by Cabinet. One of these Ministers sits as Vice-

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[176] The name C.I.C. has been retained for particular legal purposes but the corporation functions, essentially, as the C.M.B.

Chairman[177] of the board of each Crown and the C.M.B. Chairman also acts as Minister of Finance and Chairman of the Treasury Board. The C.M.B. utilizes two subcommittees, the Resources Committee (composed of four ministers and the four non-Ministers and chaired by the C.M.B. Chairman), responsible for ongoing liaison with the eight Crown corporations which operate in "competitive" markets, and the Utilities Committee (composed of four ministers and chaired by the Vice-Chairman of the C.M.B.), charged with the five non-competitive corporations. It receives its major policy direction from the Cabinet Planning Committee.

The actual monitoring mechanisms instituted by the C.M.B. will be discussed in more detail in subsection (ii), infra. For the moment, it is important to note that despite its extensive staff and broad mandate, its capacity is advisory only; the ultimate decision-maker in Saskatchewan continues to be the Cabinet[178] which must pass on fundamental items such as final approval of capital budgets, appointment of the board of directors and "politically sensitive issues." In addition, Cabinet Committees such as the Committee on Collective Bargaining will be consulted when issues within their particular expertise are involved.

Additional government players involve the Minister of Finance, who arranges borrowing for the larger Crown corporations and is, thus, also involved in capital budget approval, and the Crown Corporations Committee, an active permanent Committee of the Saskatchewan Legislature which examines the corporations' Annual Reports and reports thereon to the Legislature. It appears, however, that this Committee is some three years behind in reviewing Reports and is not seen as an effective control mechanism.

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[177] Until the institution of the C.M.B., a Minister always sat as Chairman of the board.

[178] Treasury Board Report, supra., n. 11, at p. 18.

One final player which should be noted is the new Public Utility Review Commission ("P.U.R.C."), created pursuant to the P.U.R.C. Act, S.S. 1982-83, c. 22. The Commission's general mandate includes interalia, regulation of rates charged by Sash Tel within Sashatchewan for non-competitive telephone services, rates charged by Sashatchewan Power Corporation for the sale of electrical energy and gas within the province and basic insurance premiums set by Sashatchewan Government Insurance for motor vehicles and driver's (S-3(1)). The Commission is composed of a maximum of seven Commissioners, appointed for five-year terms by the Lt. Governor in Council. Previous comments regarding duplication of effort by regulatory tribunals are at least equally applicable with regard to P.U.R.C., perhaps all the more so as as I was advised during interviews that the C.M.B. would only interact with the Commission in the event that the politicians would not want to take direct responsibility for communicating a particular decision to it (which situation has, apparently, yet to arise). Thus, to date, these two very important monitors of corporate performance have operated independently.

Thus, while Saskatchewan has, in theory, set up a single monitor of Crown corporation performance, in practice, at least seven entities are involved: the responsible Minister (who sits on both the corporate and C.M.B. boards), the C.M.B. and its Committees, the full Cabinet, additional Cabinet Committees, the Minister of Finance, P.U.R.C. and the Crown Corporations Committee of the Legislature.

The province of Quebec would, at first blush, appear to involve the least number of government monitors, owing to the key roles played by the responsible

Minister and the Cabinet, both of which are generally involved in approving corporations' "plans de developpement"[179], issuing directives, setting tariffs, approving certain large contracts, appointing directors, appointing the chief executive officers and setting their salaries, amending corporate by-laws, approving borrowing, and selecting the corporate auditor.[180]

Once again, however, additional governmental entities are involved in monitoring at certain levels. The important plan de developpement is, in practice if not de jure, put before a Parliamentary Commission (which includes representatives of both the government and the Opposition)[181] and the Ministers of Finance and of State for Economic Development are also expected to comment.[182] Borrowing must, generally, be approved by the Minister of Finance who actually retains the official designation of "shareholder" of at least one Quebec Crown (the Societe Quebecoise d'Exploration Miniere ("Soquem")). This, of course, presents an interesting anomaly, for both the Minister of Finance as "shareholder" and the Minister of Energy, Mines and Resources as "responsible Minister" attend the "Annual Shareholders' Meeting" to review the company's Annual Report which has already been submitted to the National Assembly (and which has already obtained the blessing of the Minister of Energy, Mines and Resources!).

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[179] Discussed in further detail infra.

[180] In practice, the last may be done by the board.

[181] I was advised during interviews that no plan has ever been rejected by a Parliamentary Commission, primarily because the parties involved would have been aware of the plan's contents before the informal approval stage was reached, and because the Commission, in any event, does not have formal approval power.

[182] Treasury Board Report, supra., n. 11, at p. 47. Note that it does not appear that formal "approval" from either of these is required.

In addition, Crown corporations which depend on advances or budgetary appropriations submit both their budgets and plans de developpement to the Treasury Board[183] and the Public Accounts Committee of the National Assembly receives the Auditor General's comments in his Annual Report.[184] As this latter Committee met only once in the 1979-1984 period, it is doubtful that it has much impact as a monitor of Corporate performance.

Finally, the Auditor General will play a role if he is selected as corporate auditor. If he is not so selected (as in the cases of Hydro Quebec and the Societe General de Financement), however, he will not have legal access to corporate records as we saw did the Auditor General of British Columbia.

We find, then, at least seven government players who are involved in monitoring Crown corporations' performance in Quebec: the Cabinet, the Minister of Finance, the Minister of State for Economic Development, Parliamentary Commissions, the Auditor General and, to a lesser extent, the Public Accounts Committee.

We arrive, finally, at the infrastructure in Nova Scotia, in general, a smaller Crown sector with less formal mechanisms of control.

As usual, the responsible Minister and the Cabinet play the central roles, the former involved in appointing the board and its chairman, appointing the C.E.O. and sometimes setting his or her salary, approving operating and capital budgets where those must be submitted[185], sometimes appointing auditors[186] and approving loan guarantees.

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[183] Ibid., at p. 46.

[184] Ibid., at p. 49.

There are, not surprisingly, other relevant figures. Key among these is Management Board (a Committee of Cabinet) which approves requests for grants or subsidies, the Minister of Finance, who evaluates deficit financing needs and loan guarantees before they go to Cabinet, and the Industry Committee of the provincial Legislature which appears to act in a similar capacity to the B.C. Committee on Crown Corporations, traditionally calling the C.E.O. and chief financial officer of the major corporations (such as N. S. Power Corp.) to appear on an annual basis.

In addition, at least one Crown corporation (N. S. Power Corp.) is subject to the authority of an administrative tribunal, the Public Utilities Board, which must pass on rate changes. As well, as in other jurisdictions, financial statements (although not always Annual Reports) are tabled in the Legislature and are subject to the review of the Public Accounts Committee; unlike other jurisdictions, some capital budgets are also laid before the Committee of the Whole.

Thus, Nova Scotia has no specific, statutory creation (like Saskatchewan's C.M.B.) which monitors its Crown corporations. Rather, a seemingly *ad hoc* scheme of accountability -- often involving informal communication with the Premier himself[187] -- has evolved, wherein at least six government entities act, to a greater or lesser degree, as monitors: the responsible Ministers, the Cabinet, the Minister of Finance, the Industry Committee, the Public Accounts Committee and the Committee of the Whole.

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[185] Unlike other jurisdictions, the requirement of budget approval is not systematized and varies from corporation to corporation.

[186] These are, in other cases like N.S. Power Corp., appointed by the corporate board.

[187] *Treasury Board Report*, *supra.*, n. 11, at p. 51. We will return in a moment to the involvement of the Premier.

This lengthy description of monitors in the various jurisdictions does not yet complete the picture for, in addition to the many tiers of "shareholder" already enumerated, we must add at least three more: the provincial or federal Ombudsman, government commissions and inquiries into Crown sector activities and the Prime Minister or Premier himself.

There has, until recently, been some doubt as to the extent of the Ombudsman's authority to intervene in the area of Crown corporations. The Supreme Court of Canada has, however, now held that under the British Columbia _Ombudsman Act_ which permits an investigation "with respect to a matter of administration"[188], the Ombudsman can inquire into:

> ... all conduct engaged in by a governmental authority in futherance of governmental policy — business or otherwise.... Only the activities of the legislature and the Courts [are excluded] from the Ombudsman's scrutiny.[189]

While there may be ways to distinguish the case in other jurisdictions,[190] this is at least one potential monitor who must be added to the calculus.

We noted at the outset that there have, particularly in the past ten years, been many government-initiated reports, commissions and inquiries into Crown sector activity.

Unfortunately, there is evidence that these are often not effectively utilized or implemented. For example, in his 1983 Annual Report, the federal

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[188] R.S.B.C., 1979, c. 306, s. 10(1).

[189] _Supra._, n. 3, at pp. 35 and 41, _per_ Dickson, C.J.

[190] At least one Ontario Crown corporation thinks that this can be done.

Auditor General noted that no significant progress had been made in responding to the extensive recommendations set out in his controversial Report of 1976,[191] catalyst less of improvements than of more government studies.[192] In a similar vein, we note a recent clipping from the Montreal Gazette making reference to four separate studies into Via Rail which were commissioned by then Liberal Transport Minister Lloyd Axworthy during 1983-84. When asked what became of the studies (with an aggregate price tag of $100,000.00), a highly-placed official close to current Transport Minister Mazankowski answered, "Nothing... The studies simply rearranged previously known data".[193]

As to the Prime Minister/Premiers, it is difficult, if not impossible to describe with any precision when and where they are involved in monitoring. The fact is that they are, as attested to by most corporate officers interviewed, and in a most fundamental way: one C.E.O. went so far as to say that the Premier is the only government monitor whose word has any real bearing on corporate performance.

In summary, although the different jurisdictions under study have experimented with different monitoring processes (including some attempts to concentrate the effort under the auspices of a single entity), all ultimately involve a minimum of eight "shareholder" entities, often overlapping in functional responsibility and with uncertain networks of liaison inter se. Further, each of these entities, in fact, comprises numerous civil servants who may not always be well-apprised of what it is that they are supposed to be monitoring. As Gracey notes:

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[191] Canada. Auditor Genral of Canada. Annual Report of the Auditor General to the House of Commons for the Fiscal Year ended March 31, 1983 (Ottawa: Ministry of Supply and Services, 1983) at p. 14.

[192] See, e.g., the Blue Paper, supra., n. 1. Some changes have now been implemented in Bill C-24.

[193] Montreal Gazette, February 11, 1985.

> Some of the departmental assistant deputy ministers who are charged with administering C-24 are at a loss as to how certain elements are supposed to work.[194]

Moreover, many corporate officers agreed that very few people in government really understand the difference between a Crown corporation and a government Department: as the latter is the form most familiar to them, they tend to monitor the former with reference to standards applicable to the departmental form. For example, one C.E.O. confided that the civil servants in his Minister's office are not used to using generally accepted accounting principles and have no real incentive to commence doing so.

Finally, each time the government changes, additional information and "loss-of-continuity" costs are incurred, and these may be large.

The Differences from private sector activity are apparent and comprise extra Costs of co-ordination and information gathering, extra manpower ("layering Costs") and widespread duplication of effort. As noted by Gracey:

> Control and direction by the collectivity of ministers can be no control and direction at all. The astute Crown corporation can often play one minister off against another and get what it wants. The process of obtaining approval from a host of ministers is also time consuming ...[195]

The Costs involved may be even more extensive than would so far appear, for one has yet to pose the questions: How well do the various government monitors attend to their responsibilities? What incentives do they have to do so?

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[194] D. Gracey, Record from the Strategic Planning Forum Conference (Ottawa: unpublished, October, 1984), at p. 101.

[195] Gracey, supra., n. 4, at p. 15.

The answer requires development of a general model of the factors which motivate politicians and bureaucrats and could consume an entire discussion in and of itself.[196] For our purposes, the following summary will suffice.

The 'economic model of representative democracy' views politicians as economically "rational men" who make decisions in accordance with the dictates of their own Utility functions, much as do the managers described in Williamson's model, above. Here, too, the individuals are motivated by non-pecuniary emoluments, not of pay, power, prestige and the like[197], but of votes or political support. As suggested by Trebilcock and Prichard:

> In our framework of analysis, political decision-makers have only one ultimate objective in all policy decisions — promoting their prospects of election or re-election (vote maximization).[198]

Thus, the "political market paradigm" sees the actions of politicians -- including their monitoring activities -- as a function of their desire to maximize political support. This, in turn, depends on a number of variables, primary among them being perceived voter preferences in a market characterized by high information costs.[199]

Does such a model predict active, accurate monitoring by political shareholders? I would suggest not, for the following reasons.

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[196] See, e.g., Downs, An Economic Theory of Democracy (New York: Harper and Row, 1957).

[197] See discussion infra., text accompanying n. 214.

[198] Supra., n. 6, at p. 16. See also Trebilcock, Waverman and Prichard, "Markets for Regulation: Implications for Performance Standards and Institutional Design", in Ontario Economic Council, Government Regulation: Issues and Alternatives (Toronto: Ontario Economic Council, 1978), at p. 11.

[199] Information Costs are high because voting occurs infrequently and relates to a diverse package of issues. For a fuller discussion, see Quinn, Palmer and Resendes, supra., n. 10, at pp. 391-397.

Firstly, we have the obvious problem that none of the political monitors is himself the residual beneficiary of good corporate performance, except to the extent of the portion of the total Canadian (or respective provincial) tax bill which he bears. Thus, the key incentive postulated by Alchian and Demsetz with respect to the private enterprise shareholder is lacking. As was suggested by one individual interviewed, Ministers tend, rather, to regard self-financing Crown corporations as "cheap" vehicles for accomplishing public policy objectives: the costs are "hidden" and do not represent a claim on the Minister's Departmental budget. This problem is likely exacerbated by the federal budgetary "Envelope" System (the "P.E.M." System) which, at the beginning of each fiscal year, allocates a fixed amount to each of 12 Policy Envelopes. If a Minister requires funds in any such policy area, she must go to that Envelope's Cabinet Committee and justify the project. Accordingly, there is an incentive for Ministers to find imaginative ways to bypass the Envelope; Crown corporations represent an ideal opportunity.[200]

Secondly, in the absence of a "scandal"[201], Crown corporations are unlikely to constitute a highly visible element in the package of issues facing voters at election time; this is particularly true with respect to corporate performance which occurred during the first two, or even three, years of the politician's term. This point was mentioned by a number of corporate officers.

Further, but also due to high information costs, politicians are likely to be most responsive to issues which are important to the most vocal subgroups of voters. These, in turn, will more likely focus on inflation, acid rain or women's issues than on the efficiency with which, for example, Soquem explores for new gold mines.[202]

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[200] The P.E.M. System also exacerbates the problem of inadequate dividends being paid out by Crown corporations, as we shall shortly see; the temptation is to keep the corporation's retained earning/surplus as high as possible.

[201] Hence, the relevance of the media as a monitor, discussed infra.

Finally, I would put forth the hypothesis that politicians will place greater value on the 'downside' of poor political publicity than on the upside of good publicity: the "scandal" of Canadair likely ruined the careers of more public servants than the success of Soquem has generated. As suggested by several of the corporate officers interviewed, the public is "fickle": it is the first to castigate when something goes wrong and the last to reward in the event of success. Thus political actors may well have incentives to "hide", to not take responsibility as monitors, but "pass the buck" to one of the other government entities involved; as we have seen, there are many available to pass it to. As Gracey notes:

> This diffusion of real responsibility for Crown corporations is seen by many as a fundamental defect in their direction, control and accountability.[203]

Alternatively, politicians may simply have an incentive to remain "independent" of the Corporation. As noted by Musolf:

> When queried, federal Cabinet ministers in Canada traditionally have drawn the line at answering questions on day-to-day corporate activities on the theory that they...wished to "distance" themselves, as the executive arm of government, from corporate decision making.[204]

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[202] We do not suggest that there are no subgroups in society which are concerned with the "upside" and "downside" of Canadian public enterprise, but merely that these are likely not the most visible.

[203] Gracey, supra., n. 4, at p. 7.

[204] Musolf, Public Ownership and Accountability: The Canadian Experience (Cambridge: Harvard University Press, 1959).

This "theory" is most interesting in light of the facts that, firstly, ministers are, clearly, far-from-distanced from corporate decision-making (particularly under Bill C-24) and, more importantly, it is precisely the function of the executive arm of government to monitor achievement of Other Policy Objectives.

In summary, our comparison of shareholder monitoring in the private and public sectors suggests that the layering, coordination, and information Costs described above are aggravated by the Costs associated with the Differences in the incentives facing shareholders of private enterprise and the surrogate government shareholder of public enterprise. Indeed, given the paucity of incentives to monitor and the many duties and responsibilities already assigned to Cabinet Ministers, one is tempted to query whether the "government shareholder" constitutes a monitor at all.

But what of the true residual beneficiary of public enterprise, the taxpayers whose tax bills presumably drop when Crown corporations make money and increase when they don't? Why do they not monitor Crown corporations or, within the political market paradigm, pressure the politicians they vote for to do so for them?

The response, in part, is found in the above discussion: high information costs make it difficult for voters to isolate issues relating to Crown corporations and to reward or penalize politicians accordingly, particularly if the action occurred three years before an election. As suggested by Chandler:

> Because the costs are not obvious, those who ultimately stand to lose the most from the policy [facilitating economic development — e.g. expanding industry in northern B.C.] are unlikely to oppose it.[205]

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[205] M. A. Chandler, "The Politics of Public Enterprise", in Prichard, supra., n. 2, at p. 210.

But the full answer is even more complex and flows from the fact that taxpayers probably have little incentive to pressure their M.P.'s (M.L.A.'s, etc.) to moniter well due to the "gain-splitting" nature of the public's monitoring activities. That is, why would any single taxpayer (or group of taxpayers) incur the total cost of monitoring (or of pressuring public servants to monitor) when she will benefit only in proportion to the ratio of her own tax bill to the country's (or province's)?[206]

Hence, the potential role of the press and the Opposition. Both of these (particularly the former) were cited to me in interviews as important guardians of the public interest in Crown enterprise and it is, perhaps, no coincidence that on an Air Canada flight to Toronto, on a random Saturday, I clipped three separate articles relevant to this study from the Toronto Star. No doubt, the media have adequate incentives to monitor Crown corporation performance. Equally of no doubt, this is not the monitor which most taxpayers would choose to protect their huge investment in public enterprise. We will return, in Chapter V, to a discussion of who should in the absence of adequate political or taxpayer incentives to do so.

2) The Board of Directors

The second potential monitor of public enterprise performance (i.e. of achievement of Other Policy Objectives in a cost-efficient manner) is the corporate board of directors.

We saw above that the board of the privately-owned corporation constitutes a key link between corporate management and widely dispersed shareholders, accountable to the latter for firm performance (i.e. the "bottom line"). The individuals not only have strong incentives to monitor (they likely own shares or stock options and will not be re-elected if the company doesn't "produce"); they also have probably been selected for their knowledge and expertise.[207]

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[206] For a more complete discussion of "gain-splitting", see Borcherding, supra., n. 8, at p. 129-130.

The following paragraphs will examine the boards of Canadian Crown corporations with a view to both of these variables.

It is difficult to attempt to describe the "typical" Canadian Crown corporation board, largely because there is no such thing: the nature and character of such boards from province to province and, indeed, from corporation to corporation.

All boards across the country are appointed by Cabinet on the recommendation of the responsible minister. There, the uniformity ends. In some cases, it appears that only the Minister and Cabinet are involved in the selection process. In some, corporate management is also consulted (e.g. the Canadian Development Investment Corporation ("C.D.I.C.") and Air Canada[208]), and in some (e.g. Ontario), all government ministers are "unofficially" advised that prestigious directorships are available. It seems that in most jurisdictions, the provincial Premier is, in practice, if not officially, also involved.

The actual composition of the board may vary even more. In some cases (e.g. the British Columbia Development Corporation ("B.C.D.C.") and Saskatchewan Government Insurance ("S.G.I.")), boards consist largely of business persons, sometimes retired, sometimes not, much as in the case of our representative private enterprise, although even in these cases there appear to be more lawyers and accountants than one would generally expect. The choice of other boards would seem, on the other hand, to have concentrated more on regional representation than on business expertise (for example, two of Soquem's seven board members are the mayors of small provincial cities) or satisfaction of the demands of particular political interest groups (e.g. including women on the board)[209].

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[207] Whether as businessmen, bankers or firm employees. See, e.g., the current board of Bell Canada.

[208] Note that the new Air Canada Act, 1977 has removed the old requirement of mandatory consultation.

Probably the most interesting feature of Crown corporate boards is the possibility of direct ministerial involvement at the board level. In British Columbia and Saskatchewan, the responsible minister always sits on the board; until recently, he or she always sat as chairman in the latter province.[210] In Nova Scotia, a minister may or may not sit on the Board; if not, then it is likely that at least one other civil servant does (for example, three deputy ministers sit on the ten-member board of Nova Scotia Resources[211]). This latter point is also often true in Ontario, Quebec and the federal jurisdiction where ministers do not themselves sit on the boards[212]; in most of these cases, they are nonetheless "welcome" to attend board meetings.

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[209] This might equally be the case in private enterprise.

[210] As above, the Minister now generally sits as Vice-Chairman.

[211] _Treasury Board Report_, _supra._, n. 11, at p. 52.

In contrast to the private sector, the President and Chief Executive Officer are not generally board members (although they too are "welcome" to attend meetings); exceptions occur in British Columbia (e.g. I.C.B.C. and B.C.D.C.).

Thus, board composition in the public sector differs from that found in private enterprise in that politicians and civil servants may actively be involved and in that few boards include individuals experienced in the particular product market of the corporation. This Difference from private sector activity constitutes a Cost to the corporation in terms of lost expertise and talent.[213]

How well are these boards likely to moniter corporate activity? The answer lies in our earlier discussion of managerial incentives in a corporate structure where ownership and management are separated.

We saw, above, that managers seek to maximize not firm wealth, but their own Utility functions, the elements of which may be both pecuniary and non-pecuniary. To the extent that they can be made to internalize non-pecuniary consumption, owner wealth will be increased.

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[212] For example, the Ontario Energy Corportion Act, R.S.O. 1980, c. 333, requires that the Depury Minister of Energy sit as Chairman (although he has not done so since 1981) and two Deputy Ministers sit on the board of the C.D.I.C. See also the Treasury Board Report, supra., n. 11, at p. 36. One exception is Soquem where no board members are provincial civil servants; even here, however, two directors are public servants (mayors of Quebec cities).

[213] This is not to suggest that there are not very talented individuals sitting on boards of Canadian Crown corporations. On the contrary, some C.E.O.'s positively "raved" about theirs.

In public enterprise, however, techniques such as stock options, which align managerial and owner goals, are not available. Nor, in the case of directors, are profit-sharing schemes such as that currently being considered for Air Canada employees[214].

Which, then, are the relevant variables in the director's Utility function? Niskanen suggests that these include, at a minimum:

i) pay, power and prestige
ii) ease of management, and
iii) security of tenure.[215]

What does such a theoretical framework predict with respect to the behavior of boards of Canadian public enterprises?

Pay is likely a non-issue for directors across the country tend (as in the private sector) to receive only nominal remuneration.

"Power" (or lack of it) may, however, be quite relevant. As we have already seen, the board's nominal authority to "manage the affairs of the corporation"[216] is severely constrained by the many tiers of government approvals which are required before major corporate activity is undertaken.[217] Moreover, in most cases, the board does not even have the authority to hire and fire management or set its salaries.[218] The situation may be worst in Quebec where it has been suggested that boards are relatively passive.[219] As suggested by Langford:

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[214] This will be relevant to our discussion, infra., of incentives to corporate management.

[215] Cited in Quinn, Palmer and Resendes, supra., n. 10, at p. 397.

[216] See, e.g., Bill C-24, supra., n. 12, s. 118 and Saskatchewan's Crown Corporations Act, 1978, supra., n. 35, s. 6(1).

[217] See also Section d), infra., on Corporate Authority.

> The largely bureaucratic environment of a central agency [might have the effect of] downplaying the corporate leadership of the board of directors and of, thereby, eroding the central element of the corporate firm.[220]

The problem is exacerbated by the fact that directors often don't know exactly what it is that they are supposed to be monitoring. As noted by the Wolff Commission:

> The normal function of boards of directors is to establish and moniter the authority of senior managers, within the corporation's mandate. Without clear corporate objectives, the basic information needed to offer such guidance is lacking.[221]

Thus, Crown corporate boards would appear to consume little pay and, when compared to the private sector, relatively little power. It is difficult to determine how much "prestige" or "ease of management" they command without further research. The latter is likely a problem for managing cannot be an easy task when government approvals must be sought at many levels and when time must be spent "second-guessing" what the government shareholder really wants.[222] The prestige factor poses analogous difficulty: how can a director consume prestige when she is left uncertain as to what criteria the shareholder (both government and tax-paying public) is using to judge her performance? If anything, the director's prestige is enhanced when Crown corporations are profitable, and, while profit is surely not a bad thing, it does little to influence her to monitor achievement of Other Policy Objectives.[223]

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[218] This is true for some corporations in Ontario, most in Nova Scotia (although the Nova Scotia Power Corp. board sets the C.E.O.'s salary), most in B.C. (unless the corporation's constituent Act states otherwise) and probably all in Quebec (with the guidance of the Secretaire General Associe aux Cadres Superieurs, a senior official).

[219] Treasury Board Report, supra., n. 11, at p. 45. Note that corporate officers in the two Quebec Crowns which I interviewed did not support this view.

[220] J.W. Langford, "Crown Corporations as Instruments of Policy", in B.G. Doern and P. Aucoin, Public Policy in Canada (Toronto: Macmillan, 1979) at p. 265.

[221] Wolff Commission Report, supra., n. 1, at p. 5.

The possible incentive of ensuring security of tenure also does not give us much leverage with respect to motivating directors to monitor corporate performance. Firstly, it is doubtful that "keeping the job" is of great import to directors when the pay and prestige factors rank so low and the frustration factor so high. Secondly, the fact is that, except when there is a change in government, directors of Crown corporations are rarely asked to resign; one C.E.O. confided that his government has often forgotten to replace directors even when their terms are up. Thus, this potential incentive to effective monitoring is also not well-utilized in the public enterprise sector.

Where does this leave us with respect to directors' propensity to monitor achievement of Other Policy Objectives at least cost? Probably with little hope as there do not appear to be any factors which directly align direc-tors' incentives -- pecuniary or otherwise -- to this goal.

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[222] See discussion, infra., on specification of objectives.

[223] In interviews, this factor was quoted more often than any other as the relevant measure of success and I expect that that is at least equally true with respect to media coverage and political evaluations of directors' performance. The possibility that high profit margins provide a major (if not the major) incentive for directors and management will form an important theme in the succeeding discussion.

One further point. Nearly all jurisdictions evidenced a trend to replace all or most of the board when a new government takes power. For example, many boards in Saskatchewan were "wiped out" when Premier Devine took over in 1982 and the recent Conservative victory in Ottawa has led to significant (or total) changeovers in the boards of C.D.I.C., Petro Canada, Via Rail Ltd. and Air Canada. While it is true, as one senior officer suggested to me, that it is "normal" for a board to change when a new shareholder takes control, one must remember that the "new shareholder" in this case remains the representative of the same constituency -- the Canadian taxpayer -- and that to each total changeover in a board there corresponds a large Cost in terms of lack of continuity and re-education of the parties involved (both existing management and the new directors). Moreover, it seems unlikely that the entire board would ever be changed in our representative, widely-held private sector company, let alone potentially once every four or five years.

This practice of reconstituting the board suggests one of two things: either such changeover reflects a complete turnabout in Other Policy Objectives which necessitates a new set of monitors, or the board is, to some extent at least, a political creature rather than a true monitor of corporate performance. While it is impossible empirically to determine which, I would suggest that as Other Policy Objectives are poorly defined to begin with (see infra.), it is unlikely that the former possibility governs.

3. Corporate Management

The third and final potential monitor of Crown corporation performance is corporate management itself.

In contrast to the public sector "shareholder" (which we found to consist of many layers, not always acting in tandem with one another) and board of directors (selected on the basis of uncertain criteria, facing little threat of dismissal or censure), the character of Crown corporate management does not appear to diverge significantly from that found in the private sector. Some Differences do, however, exist.

Firstly, managers of Canadian Crown corporations come from relatively diverse backgrounds. Many were trained in the private sector but perhaps equally many rose through the ranks as telephone men or airline people. This latter group would not fall within the strict definition of the "professional manager"; as many private enterprise corporations also select their management from within, I do not identify this alone as the source of a Cost.

In some cases, however, senior civil servants have entered the ranks of corporate management -- examples occur in at least Saskatchewan, Ontario and British Columbia where the Premier was the President of B.C. Rail prior to 1978 -- generally because, as one individual stated in an interview, the corporations have not paid sufficient salaries to attract business people. We will return to the issue of remuneration in a moment. For now, the important point is that the practice of using civil servants as managers may generate Costs in terms of sheer lack of expertise, no matter how talented the individual.

The second Difference which emerges is that the Chief Executive Officers of most Canadian Crown corporation are appointed not by the board of directors, but by Cabinet or the responsible Minister, thereby making the officer accountable to a political rather than a corporate monitor.

Finally, as in the case of the board (and as we shall see more fully in section d) below), management of Crown corporations has far less discretion regarding corporate decision-making than it would in the private sector.

The Costs which emerge from such Differences are similar to, if less apparently severe than, those identified above in our discussion of the public enterprise board: layering and co-ordination Costs, duplication of effort and potential lack of expertise.

Even more critical here is the fact that management has not been given incentives designed to minimize the Costs associated with monitoring Other Policy Objectives.

In this context, we return to the Niskanen model sketched earlier,[224] which viewed pay, power and prestige, ease of management and security of tenure as the relevant elements in managers' Utility functions and add 'future marketability in the managerial labour market' to the list.[225]

The general consensus of opinion among the corporate officers interviewed was that top management (although not less senior management) in the Crown sector is paid as much as 50% less than it would be in private enterprise. It was suggested during one interview that this was due to the propensity of government to view public sector managers as public servants of essentially the same level as Deputy Ministers and, accordingly, of the same pay "classification".[226]

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[224] Supra., text accompanying n. 214.

[225] This is implicitly suggested by Fama, supra., n. 138, at p. 58.

[226] This "standard" is applicable in some jurisdictions and with respect to some company's within them (e.g. remuneration of the chairman of Ontario Hydro), but not to others where salaries may be based on a percentage of industry average (e.g. remuneration of the President of Ontario Hydro) or on the "unknown" guidelines (e.g. Air Canada).

Moreover, senior officers cannot hold corporate shares or stock options as they likely would in the private sector, although it is noteworthy that Air Canada is contemplating institution of a profit-sharing plan in which management will participate along with other employees.

Finally, management of Crown corporations may find itself subject to legislation concerning public sector wages and salaries. For example, managers of British Columbia Crowns have for several years had their salaries frozen under the Compensation Stabilization Act[227]; I am advised that at B.C. Rail salaries of senior executives have been frozen for 3 1/2 years and the President's for even longer.

Such practices generate a Cost in terms of reducing the potential pool of talented managers from among which corporate management can be selected. Further, they affect the "pay" variable in management's incentive structure by not permitting adequate flexibility to increase salaries when Other Policy Objectives are achieved (i.e. to reward good performance) or to otherwise tie managerial remuneration to corporate performance.

Similar Differences prevail when one examines the "power" and "prestige" variables. As was noted above, management of Crown corporations retains relatively little discretion with respect to corporate decision-making; this has direct influence on the "power" variable within the calculus. The prestige element is even more problematic; one senior officer confided that government attaches relatively little importance to Crown corporation managers and that they consequently had to find satisfaction "from within". Thus, neither factor ties directly into achieving Other Policy Objectives.

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[227] Supra., n. 111.

Nor does ease of management. Indeed, many corporate officers revealed that their most difficult problems concern attempting to figure out how government wants them to manage their companies and frustration arises when decisions which have passed through corporate boards are overturned by Cabinet Ministers.

Further, I would suggest that ease of management of a Crown corporation likely varies inversely with the amount of contact had with the government shareholder; that is, managers' lives are easier when they are left to do their jobs "in peace". This point was often volunteered in interviews (one officer saying, "I wish to ---- that they [government] would just tell me what they want me to do so that I could go ahead and do it for them") and is anticipated by Gracey when he states:

> [When many government entities must be dealt with in order to make corporate decisions], managers feel that they are being "second-guessed" by ministers and bureaucrats and resist meaningful dialogue with ministers and departments lest that dialogue lead to further second guessing.[228]

That is, one might hypothesize that rather than trying to expedite government monitoring, managers have the incentive to convey to government as little information as possible; a recent study by Dr. Litvak of York University concludes that, indeed, the standard of disclosure is lower in public than in private corporations.[229] Such incentives will obviously work in direct antithesis to our goal of monitoring Other Policy Objectives at least cost.

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[228] D. Gracey, "Public Enterprise in Canada", in Gelinas, supra., n. 2, at p. 32. See also C.H. Hindle, "Practical Problems in the Evaluation of Crown Corporation Performance" (Regina: Crown Management Board of Saskatchewan, submission to the MacDonald Royal Commission Symposium on Crown Corporations, June, 1984), at p. 2, where he states: "A corporation's ... management generally act[s] to ... increase its autonomy by reducing dependence either on outside resources or outside decisions."

The security of tenure variable could, in theory, provide a prime opportunity to align the manager's objective to keep his job with an incentive to achieve Other Policy Objectives at minimum cost. There is no evidence, however, that this has been done; managers felt that, if anything, tenure is tied to corporate profitability and avoidance of "scandal", much as did directors. Moreover, tenure is generally, as above, determined by Cabinet or the responsible Minister (rather than the board) at least one step removed from managers' actual performance.

Finally, there appears to be relatively little turnover in corporate management. Even where management is ultimately dismissed for "poor performance" as in the case of Canadair, the shareholder, in the opinion of one C.E.O., waits far longer to do so than would the private sector (Canadair lost approximately $1.4 billion before management was changed). As suggested by another C.E.O., "Government has never really concerned itself with the management of its managers and the board is powerless to choose [us] or fix [our] remuneration."

The final variable, the desire of managers to maintain a high rental rate in the managerial labour market is intimately linked to current salary and benefit packages (as above, low at top levels of Crown management) and to their reputations as "successful" businessmen. The latter again could provide government with an opportunity properly to align managerial incentives if it were to ensure that "success" be well-defined as "achieving Other Policy

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[229] Cited in Gracey, supra., n. 194, at p. 101.

Objectives at least cost" and if it were equally well to reward good performance (if not in pay, then, at least in prestige and publicity). There was no evidence put forward during interviews suggesting that this has been done. Rather, as noted by Gracey:

> The success of a chief executive officer springs usually not from his business skills but from his "small 'p' political" skills -- being able to manoever around the rocks and shoals of the political and bureaucratic world.[1]

That is, managers of Crown corporation probably face greater incentives to appease the government monitor (in accordance with the latter's vote-maximizing Utility function) than to monitor corporate performance.

In summary, as concluded by Quinn, Palmer and Resendes in their excellent case study of Gray Coach Lines:

> Public managers are less likely than their counterparts in private firms to bear costs or internalize rewards from profitable performance.[2]

Absent altruism, it is unlikely that they will have adequate incentives to monitor corporate performance of Other Policy Objectives.

This section has illustrated the fact that Differences exist with respect to the relative costs of monitoring corporate performance in the private and public sectors by all three groups of potential monitors. Layering, co-ordination and information Costs run high in all cases, and particularly with respect to the government shareholder. There is little overt encouragement to choose directors/managers with maximum expertise (although there are many talented individuals in the public sector). Finally, and I would suggest, most importantly, the institutional infrastructure is not designed with an eye to the objective of linking the goals of these monitors with the ultimate goal of public sector enterprise: achieving Other Policy Objectives in the most productively-efficient manner.

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[1] D. Gracey, Speech Notes for I.P.A.C. (Ottawa: unpublished, 1984), at p. 9.

[2] Supra., n. 10, at p. 397.

The next subsection will go on to describe how monitoring is effected and what Costs are therein involved.

ii) Reporting Techniques

Reporting requirements in our representative private firm are specific and well-defined. Management reports formally to the board perhaps quarterly and somewhat more often on an informal basis; neither of these requirements is statutorily mandated. Apart from extraordinary corporate activity (such as a pending takeover bid which requires that a Directors' Circular to be sent to shareholders -- C.B.C.A., s. 194(1)), the board need then report exactly once to its shareholders -- by way of an Annual Report containing approved Financial Statements and an Auditor's Report.[3]

The situation in the private sector is, as we have by now come to expect, far more intricate and far more "layered". The relevant techniques include not only the specific financial controls which will be described in the following paragraphs (capital and operating budgets, audits, Annual Reports, and control over borrowing) but also the mechanisms more fully described in subsection (iii) as instruments of objective specification (corporate plans/plans de developpement/Memoranda of Understanding, government directives, informal discussions with the responsible Minister, etc.).

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[3] C.B.C.A., supra., n. 22, ss. 149(1), 152(1)

1) Budgets

It appears generally to be agreed that government's key control (or, in our language, monitoring) mechanism over Crown enterprise is financial: budget approval and control over borrowing.

Requirements for submission of budgets vary across the country. All jurisdictions (except Quebec and British Columbia) require that capital budgets be approved (at least in terms of the absolute dollars to be expended[4]) and few require that operating budgets formally be approved (although, as we shall see shortly, some require that they be submitted for "informational" purposes).

There, the similarities end. In British Columbia, the above-mentioned Fiscal Agency Agreements usually require that capital budgets be submitted to the Minister of Finance "for information purposes"[5]; the value of such monitoring is difficult to assess as no formal approval is required and at least some B. C. Crowns view their capital budgets as being approved by their boards rather than the government. In Saskatchewan, capital budgets go to the C.M.B., implicitly having obtained the approval of the responsible Minister who sits on the corporation's board. The Department of Finance does not participate officially but informal consultation normally occurs before the budget goes to Cabinet. In Ontario, under most Memoranda of Understanding, the capital budget goes to the Minister for approval[6] but not to Cabinet or the Legislature. In Quebec, no approval at all is formally required although if the corporation submits a plan de developpement, the capital budget will be included therein; as we shall see below, at least some plans are not approved for several years after submission. In Nova Scotia, the budget control mechanism varies from corporation to corporation. Some must obtain the approval of the responsible Minister and Management Board (a Cabinet committee) and some (like the Liquor Commission) have no reporting requirements at all.[7] At the federal level, on the other hand, s. 131 of Bill C-24 sets out a fairly rigid scheme which requires that Treasury Board approve the capital budget of each parent Crown corporation following the recommendations of the responsible Minister and, in his own discretion, the Minister of Finance (s. 131(7)). In addition, the corporation must submit a summary of the budget for ministerial approval and tabling in Parliament; usually this is included within the corporate plan summary, described infra. (s. 132)

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[4] We shall see shortly that there is, in practice, a fair degree of "juggling" within the overall budget.

[5] Treasury Board Report, supra., n. 11, at p. 8. See, for example, Memorandum of Understanding dated September 28, 1982 between B.C. Rail and the Minister of Finance (the "B.C. Rail Memorandum"), s. 4.1.

[6] Treasury Board Report, supra., n. 11, at p. 54.

Thus, the governments' various systems of monitoring capital expenditures of Crown corporations run the gamut from the fairly loose scheme in Quebec to the rigid approach of Bill C-24. Not only is there a Cost implicit in the fact that so many different techniques are used (they can't all have found the most cost-efficient method), but the very efficacy of the budget approval process has been queried:

> In several cases, the quality and integrity of budgets have been such that they do not adequately inform Ministers or Parliament of the capital or operating plans of Crown corporations or their long-term implications. In such cases, budgets are largely ineffective as instruments of accountability and control.[8]

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[7] Memorandum of Understanding entered into between the Minister of Energy and the Ontario Energy Corporation dated September 20, 1984 (the "O.E.C. Memorandum"), ss. 9.1, 9.2.

[8] Gracey, supra., n. 228, at p. 32.

Further, it appears that government tends to be somewhat delinquent in reviewing budgets. For example, during fiscal 1982, at the federal level, only two Crown corporations had their budgets approved before the beginning of their fiscal years. Three per cent were approved after the year to which the budget applied and 25% were never approved at all.[9] Gracey also cites the example of a Crown corporation whose budget failed to receive approval and which had to supply government with more information concerning it: approval was finally obtained, but only after the end of the year to which it applied and after many of the commitments in the budget had already been undertaken.[10]

Finally, it seems that even if approval has been obtained, Crown corporations are relatively free to "juggle" funds within it, provided that the total does not vary significantly:

> Once their budgets have been approved by the government, several Crown corporations have made significant transfers within budgets, exceeded budget ceilings or entered into expenditures and commitments not provided for in any approved budget.[11]

At least the former practice was confirmed during the course of my interviews.[12]

We find, therefore, a potentially major Difference from private sector activity: not only must capital budgets be approved (a Cost in and of itself), but the effectiveness of such approval in monitoring corporate behavior is suspect, potentially a "deadweight" Cost.

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[9] Auditor General of Canada, supra., n. 149, paras. 2-120 and 2-121.

[10] Gracey, supra., n. 228, at p. 32.

[11] Ibid.

[12] This is not to suggest that such flexibility is bad, but merely that it detracts from the viability of budgets as a monitoring mechanism.

Operating budgets, as suggested above, receive different treatment: in no jurisdiction do they require formal approval. However, several provinces do require that budgets be submitted "for information purposes". For example, corporations accountable to Saskatchewan's C.M.B. submit operating budgets along with their strategic plans and many Ontario corporations do so pursuant to their Memoranda of Understanding.[242] Similarly, certain Nova Scotia corporations (e.g., Sysco) must, under their constituent Acts, submit an operating budget to the Minister of Finance who "signs it off" and B.C. Ferry Corp. must submit such budgets to the provincial Cabinet.[243]

Again, there is a clear Difference vis-a-vis the private enterprise corporation. Further, it is very difficult to determine what, if any, use is made or purpose served by submission of such operating budgets and whether it is not, consequently, merely a deadweight Cost.

2) Audits

Crown corporations in all jurisdictions must submit audited financial statements to Parliament or the provincial Legislature, usually along with their Annual Reports (discussed infra). The auditor may come from the private sector (e.g. Ontario Hydro, Potash Corporation of Saskatchewan) or may be the Provincial Auditor or Auditor General (e.g. Soquem, Expo '86, Saskatchewan Government Insurance). In the case of the commercial-type Crowns being discussed here, the former is usually used.

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[242] See, e.g., the O.E.C. Memorandum, supra., n. 236, Article 9.

[243] Treasury Board Report, supra., n. 11, at pp. 53 and 8, respectively.

So far, no Differences emerge. The first potential one of note is that the choice of private auditor may be made by different entities in different jurisdictions -- by the Cabinet on the recommendation of the responsibleminister (the federal jurisdiction (Bill C-24), sometimes in Nova Scotia and Saskatchewan), the corporate board of directors (e.g. Quebec, sometimes Saskatchewan) or the Minister of Finance (e.g. B.C. Place[244]). It is difficult to determine whether or not this Difference actually results in a Cost, i.e. whether any of these four entities is less cost efficient than shareholders of a privately-owned corporation in choosing auditors. Probably not, and, accordingly, we do not identify a Cost here.

A more important Difference from the private sector does arise, however, due to the fact that in most provinces and at the federal level, the government's auditor has the power to become involved even if an outside audit has been performed, either by having access to the books, records and audit reports (e.g. Ontario, Saskatchewan) or by actually reviewing the outside audit and, if necessary, expanding its scope (e.g. Nova Scotia, British Columbia). Or, he may simply decide to review certain Crown corporations in his Annual Report to Parliament. While such involvement by Auditors General has often sparked needed debate over the control and accountability of Crown sector corporations[245] it also represents a great deal of time and money spent performing "double duty": if Price Waterhouse's audits are considered satisfactory to Canadian investors and provincial Securities Commissions alike, why not to the government? Further, many argue that the Auditors General have gone far beyond Parliament's intent in reviewing the Crowns. Perhaps the best example is the currently pending litigation between Auditor General Kenneth Dye and the federal government to force Ottawa to show him confidential Cabinet papers regarding the 1981 takeover of Petrofina Canada Inc. (now Petro Canada). Associate Deputy Justice Minister Ian Binnie has stated that Dye is attempting a "parliamentary bypass operation" and acting as the leader of "an extra-parliamentary non-elected opposition", trying to gain access to information which Parliament never intended him to see.[246]

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[244] Treasury Board Report, supra., n. 11, at p. 8.

[245] Perhaps the best example is the federal Auditor General's 1976 Report which catalysed a new era in studying Crown corporations; supra., n. 1.

The situation raises some very interesting questions. Is this extra monitor necessary, or, indeed, useful, in the context of Other Policy Objectives when he clearly is not operatin~ in tandem with the government? Is the no doubt hefty Cost of the Dye lawsuit justifiable in terms of monitoring Other Policy Objectives? That is, while it is true that any shareholder of a private corporation may bring in his own auditor, he must do so at his own expense, presumably an adequate disincentive to frivolous audits; the same is not true here.

We shall not comment on the issue of whether or not Auditor General Dye's allegations are justified. The important point in our context is that additional audit and inquiry functions performed by Auditors General represent a Cost which must be allocable to achievements of Other Policy Objectives if they are to be justified.

The third and most important identifiable Difference between private and public sector audits is the scope of the audit itself. In many cases where outside auditors are used, an "Auditor's Opinion" is given in accordance with generally accepted accounting principles just as in the private sector (e.g. Ontario Hydro); this may also be true where the Provincial Auditor is used (e.g. S.G.I.). In B.C., however, it appears that audits of all Crown corporations are "attest audits" and that a changeover to comprehensive auditing has been discussed by the Treasury Board and the Office of the Comptroller General but not yet implemented.[247] Similarly, in Ontario, comprehensive auditing has not been introduced although when the Provincial Auditor is used (for nine out of the 15 Schedule II Agencies), he may also undertake a "value for money" audit, i.e. to report on "any expenditure of money made without due regard to economy and efficiency or [on] where procedures to measure and report on the effectiveness of programs are not established or are deemed unsatisfactory."[248]

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[246] The Toronto Star, March 9, 1985.

It is difficult to assess how acute this Difference really is: one individual interviewed claimed that commercial Crown corporations use the same accounting and auditing standards as does the private sector, and another confided that he wished that civil servants would get used to using generally accepted accounting principles. Fortunately, accounting is outside my area of expertise and I will not, here, conduct an extensive study of the relative merits of the different methods. At minimum, it can be said that the Difference of lack of uniformity exists on both an inter- and intra-jurisdictional basis; this translates into both time spent interpreting financial statements ("interpretation Costs") and potential deadweight Costs if the statements are therefore neither used nor useful. As stated by Langford and Huffman:

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[247] Treasury Board Report, supra., n. 11, at p. 9.

[248] See Ibid., at p. 39, and Ontario Management Board of Cabinet International Audit. (Toronto: CPS Management Series) 1981, at p. 7.

> The plethora of accounting formats combined with reporting omissions and obfuscations create a comparative environment which is confusing and open to wide discretionary interpretation.[249]

3) Annual Reports

The third reporting mechanism used by the government shareholder of Crown corporations is the Annual Report, required in nearly all jurisdictions to be tabled in Parliament or the Legislature on the recommendation of the responsible Minister; the exception is Nova Scotia where the financial statements of Crown corporations are tabled as part of the Public Accounts).[250] Once there, the Report is usually sent to a Committee (such as the Public Accounts Committee or the old Committee on Crown Corporations in British Columbia) for review and corporate officers may be asked to appear for questioning.

On its face, this process does not seem very different from that of the private sector where Annual Reports and audited Financial Statements form the keystone of corporate monitoring by the shareholders. The one identifiable problem concerns the use made of the Reports. That is, while those of the major Crowns are well scrutinized, it was suggested in interviews that inadequate review is made of the less prominent corporations. Such a conclusion would be consistent with the model of politician's incentives presented above which suggested that politicians, motivated largely by maximizing votes, will focus on issues (viz. corporations) which are highly visible or politically sensitive. If this is the effect, then the ultimate Cost to society of inadequate monitoring of such corporations may be very high, and the corporations involved will have incurred wasted Costs in preparing the Reports.

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[249] Supra., n. 23. at p. 289.

[250] Treasury Board Report, supra., n. 11, at p. 62.

4) Quarterly Reporting

In addition to the formal techniques above-described, many Crown corporations across the country require that quarterly financial statements be submitted to the appropriate government authority. For example, Saskatchewan's C.M.B. requires that all Crowns submit such reports as does B.C.'s Minister of Finance pursuant to Fiscal Agency Agreements.[251] And s. 153.1 of Bill C-24 requires that the President of the Treasury Board lay such documents (the accuracy of which must be attested to by the Auditor General in his annual report) before Parliament.

The process is clearly costly and is generally only completed in the private sector in the form of a less formal quarterly report to the board alone. Further, quarterly reports do not usually relate to Other Policy Objectives, and likely duplicate at least some materials already submitted or pre--approved in capital or operating budgets, Annual Reports, or corporate plans: there is only so much that can happen every three months. Hence, yet another Cost arises.

5) Special Examinations

S. 143 of Bill C-24 introduces yet another level of federal Crown corporation reporting. Every five years, each parent Crown must cause a "special examination" to be performed, generally by its auditor (s. 144(1)), to determine if the financial, management and information control systems and practices prescribed in s. 138(1)(b) of the Bill were appropriately maintained.

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[251] See, e.g., the B.C. Rail Memorandum, supra., n. 234, s. 4.

As the Bill is so new, we have no evidence, as yet, of how useful such an examination will prove. One thing is certain: it will clearly consume ample corporate and government resources which would not be expended in a privately-owned company. That is, distinct Costs arise which must, as usual, be justified by Other Policy Objectives.

6) Corporate Borrowing

This subsection could equally be placed within the section on "Corporate Authority", infra, but we examine it here as borrowing is generally considered along with capital budget approval to form the primary control on Crown corporate performance: as one corporate officer noted, "He who controls the purse controls the operation."

Every jurisdiction under study exercises control over corporate debt, either by borrowing on behalf of its Crowns (e.g. Saskatchewan) or by encouraging approved financing in private sector capital markets (e.g. Quebec, Nova Scotia, federally) with or without a government guarantee.

As in the case of capital budget approval, the similarities among jurisdictions end there. At first blush, this should not be surprising for control over borrowing is really nothing more nor less than the final link in the capital budget approval process: if capital budget approvals are conducted differently, so too should be borrowing approvals, for it would be at least questionable practice to approve a budget and then not approve the borrowing of the funds necessary to implement it.

Yet the fact is that the hierarchy involved in borrowing approvals does not always mirror that in place for the capital budget. For example, in Saskatchewan, as we saw above, capital budgets go to the C.M.B. and Cabinet; if borrowing is anticipated, however, the Minister of Finance will also be involved. In Ontario, Schedule II corporations' budgets do not generally go to Cabinet but, under most Memoranda of Understanding, the corporations must secure Cabinet's approval to anticipated borrowing and advise the Provincial Treasurer thereof.[252] In Quebec, there is no formal requirement for budget approval (although it is usually included in the plan of development), but Cabinet approval of borrowing, following the recommendations of both the responsible Minister and the Minister of Finance must generally be obtained.[253] Similarly, in Nova Scotia, the *Finance Act* (Part IX) requires that Cabinet approval be obtained for any "funded obligation" (essentially, one maturing more than one year hence) even though it need not always be obtained for the capital budget.[254] Finally, at the federal level, the timing, terms and conditions of capital market borrowing must be approved by the Minister of Finance[255] even though it is Treasury Board and the responsible Minister (and, possibly, Finance[256]) who approve the budget.

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[252] *Treasury Board Report*, *supra.*, n. 11, at p. 38.

[253] Quebec corporations may sometimes borrow without authority up to a prescribed ceiling. These, however, are usually very low. For example, Soquem may only borrow without authority until it s total debt reaches $50,000.00. It was suggested to me that $100,000,000.00 would be a more reasonable figure.

[254] *Treasury Board Report*, *supra.*, n. 11, at p. 54.

[255] Gracey, *supra.*, n. 4, at p. 7.

[256] Bill C-24, *supra.*, n. 12, s. 131.

This lack of synchronization evidences a distinct Cost in terms of potential duplication of effort, miscommunication and lack of coordination.

The Cost is even more apparent when one recalls that in the private sector, shareholders would not monitor borrowing at all: under s.183(1) of the C.B.C.A., the directors are empowered to borrow money and give security without shareholder authorization unless the Articles, by-laws or a unanimous shareholder agreement state otherwise.

Futhermore, the fact is that many of the commercial-type Crown corporations under review in this study may not borrow that often. Rather, as in the case of private enterprise, they may attempt to finance many projects out of surplus or retained earnings. Indeed, if the literature concerning private sector corporations is applicable in this context (and, if anything, it may be even more applicable here, given public managers' incentive to operate as independently of government as possible), managers are likely to attempt to finance the replacement or expansion of corporate assets internally and to resort to capital markets only if absolutely necessary.[257] Further, given Ministers' possible incentive to not dip into their "own" funds (i.e. Departmental Funds or the appropriate Policy Envelope at the federal level), corporations may well be encouraged to finance projects internally.[258] Thus, the Cost of achieving Other Policy Objectives may remain hidden despite the official edict that borrowing be controlled; that is, control over borrowing may not, in fact, be a very effective monitoring technique.

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[57] See, e.g., V. Brudney and M. A. Chirelstein, Corporate Finance, 2nd ed. (Mineola: The Foundation Press, Inc., 1979), at pp. 441 and 450.

[58] This discussion is very relevant to that below regarding payment of dividends and access to "cheap money".

It is difficult clearly to describe the Cost associated with such "government bypass" operations: if anything, it brings Crown corporation activity more into line with the private sector. One must, however, remember that it is not profit but Other Policy Objectives (achieved at least Cost) which we are ultimately concerned with. Thus, if Crown corporations do finance internally (and a proper study of this is beyond the scope of this paper), then the information Costs attaching to monitoring such achievement may be enormous. The Cost involved is that associated with "hidden Costs" and we shall confront it again shortly when we turn to a discussion of divided payments and the corporations' Cost of capital.

7) Other Methods

There are several other methods which the government shareholder uses to monitor corporate activity. Primary among these are inquiries by Legislative Committees and so-called "informal" monitoring.

The former is perhaps best exemplified by the efforts of the (now-defunct) B.C. Committee on Crown Corporations whose most potent weapon was its power under s.3(3) to compel the attendance of corporate officers to answer questions concerning Annual Reports.[259] It could also, under S.8, compel the attendance of witnesses and the production of records as can the House or the Speaker under the *Legislative Assembly Privilege Act*.

The Committee concentrated its efforts on B.C. Hydro in 1977-1979, B.C. Ferry Corporation in 1979-1980, B.C. Rail through 1981 and had commenced its review

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[59] *Crown Corporation Reporting Act*, *supra.*, n. 169. It is interesting to note that while s.2(1) of the Act refers to the Committee's mandate to examine both officers and directors, s.3(3) only names the former.

of I.C.B.C. when it ceased operation. It held public hearings in all cases and covered topics ranging from corporate operations, to employee relations, to traffic safety in British Columbia. Each corporation was to be reviewed every three to four years. In addition, the Committee and its staff attempted to monitor many aspects of the companies' management and operation on a regular basis by means of private meetings with corporate directors and officers.

Certainly, the Committee's coverage was thorough. The suggestion, unfortunately, has been made that perhaps it was too thorough and, accordingly, too costly. As Gillian Gillespie of the Ontario Management Board points out:

> . . . The questions asked by the Crown Corporations Committee were not that different from those asked by other ongoing committees of the Legislature. When the B.C. Ferry Corporation was under consideration, for example, there was a much stronger emphasis on specifics such as the rationale for particular fares and particular routes and the levels of service, than on general questions relating to management, to economy and efficiency, and to long-term capital investments.[260]

And, although Ms. Gillespie does not mention it, I would suggest, to achievement of Other Policy Objectives set by the British Columbia government and which justify the use of the public enterprise form. Moreover, in the eyes of the Committee itself, its mandate was one of inquiry (and, perhaps, of monitoring "commercial goals") and not of monitoring nor specification nor clarification of Other Policy Objectives. The Committee had no authority over either the original corporate mandate (e.g. as set out in the corporation's authorizing legislation) or the ongoing budgets and activities of the corporations; these monitoring tasks belonged to other government players such as the responsible ministers and the Cabinet. Perhaps most importantly, the Committee was viewed

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[60] Gillespie, *supra.*, n. 162, at p. 10.

by many senior officers in B.C. Crown corporations as "good guys, trying hard, but doing little".

This is not to criticize the efforts made by the Committee. It did, however, appear to generate a Cost, the by-now-familiar one of lack of coordination and possible duplication of effort.

We will not canvass specific efforts made by other Legislative Committees (such as the Public Accounts Committees); many have been noteworthy and all were well-intentioned, but the Costs remain, nonetheless.

Finally, to the many informal methods of monitoring corporate performance: informal discussions with the Minister, breakfast meetings with the Premier, etc. As an example, we examine some of the activities of Saskatchewan's C.M.B.

The C.M.B. is intimately involved in day-to-day activities of the corporations under its jurisdiction. I am advised that memoranda are sent to C.E.O.'s regarding, for example, what type of charitable donations they should make and what types of cars corporate executives should buy. The Board has what has been described as a "huge" administrative staff and at least some corporate officers are not quite sure what they do but read the "reams of reports" which the corporations prepare in order to satisfy their "apparent appetite for paper". Expertise developed within the C.M.B. in administrative areas (such as economic forecasting) is considered to duplicate expertise already developed within the corporations and the administrative staff is seen as being much larger than would be the analogous staff in a private sector holding company. One individual confided that he would like to know what it costs to run the C.M.B., but that it was impossible to find out.

The efficacy of such techniques is obviously virtually impossible to measure as is the Cost of the effort. There is little doubt, however, that the latter is higher than would be found in our widely-held private enterprise and, hence, represents a Cost within the definition used here.

In summary, we find that the various reporting techniques used to monitor corporate performance exhibit the following Costs:

A) potential layering, duplication of effort, and coordination Costs (budgets, quarterly reports, special examinations, borrowing, Committee inquiries, Auditor General inquiries and informal monitoring),

B) potential outright waste (operating budgets, Annual Report for smaller companies),

C) interpretation Costs (audits, financial reporting in general), and

D) Hidden Costs (borrowing).

Further, these Costs relate to methods of measuring financial performance rather than Other Policy Objectives.

These concerns are buttressed by evidence that despite the use of all of these mechanisms, Crown corporations may disclose less than do corporations in the private sector.[261] Such evidence is consistent with our hypothesis that management of Crown corporations may have the incentive to keep as much information as possible from government to as to maximize its "ease of management". If so, then the Costs may be even larger than already suspected.

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[61] Gracey, *supra.*, n. 4, at p. 101.

iii) Specification of Corporate Objectives

The two preceding subsections have described the various entities which monitor Crown corporate performance and the main techniques by means of which such monitoring is instituted.

Monitoring, however, is bound to be costly (perhaps infinitely so) unless both the corporation and the designated monitors know what it is that the enterprise is supposed to be trying to do. This subsection will, accordingly, examine how corporate objectives are specified in the public sector and what Differences exist vis-a-vis private enterprise.

The private sector benchmark here is quite straightforward: firms are in business to make money, to maximize profits (both short and long term) or, alternatively, to maximize the present value of the owner's equity shares. This is true even if other objectives tied to being a "good corporate citizen" are introduced into the calculus. The objective is well-defined and is known to all parties involved. The information Costs are, accordingly, low.

The situation facing public enterprise is markedly different. As we suggested at the outset:

> One must assume that to a greater or lesser extent, every Crown corporation is intended to maximize some set of policy objectives in addition to, and indeed in opposition to, profits. If this were not so, it is difficult to conceive of any reason for a Crown corporation to exist.[262]

Clearly, management of a Crown corporation will not "simply know" what these firm objectives are, as it would in the private sector. Rather, they must be communicated and such communication will necessarily generate some Costs, justifiable Costs. The trick is, however, to ensure that these Costs are

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[62] Trebilcock and Prichard, supra., n. 6, at p. 37.

minimized, i.e. that the corporate mandate is described to the enterprise in as clear and accurate a manner as possible. Yet, when queried, nearly all corporate officers interviewed cited lack of specification of corporate objectives as the single most important problem facing Canadian public enterprise today. This result is borne out in the findings of Saskatchewan's Wolff Commission:

> The Commission frequently found the documented objectives of Crown corporations to be inappropriately defined. Consequently, there is uncertainty about the specific purposes and goals of particular corporations.[263]

The following paragraphs will examine the mechanisms currently in place for communicating Other Policy Objectives to Crown corporations and will identify the Costs associated therewith.

1) Objectives in Empowering Legislation

When queried on this subject, corporate officers tended first to cite their empowering legislation as the purveyor of the government's goals. In some cases, this may be a valuable source. For example, s. 6 of the Ontario Energy Corporation Act[264] states:

> Corporate objects 6. The objects of the corporation are,
>
> (a) to invest or otherwise participate in energy projects throughout Canada or elsewhere in order to,
>
> (i) enhance the availability of energy in Ontario,
>
> (ii) stimulate exploration for and the development of sources of energy,

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[263] Supra., n. 1, at p. 4.

[264] R.S.O. 1980, C. 333.

(iii) stimulate expansion of the capability to produce energy.

(iv) encourage investment in energy projects and the effective use of financial, human and other resources in energy projects, and

(v) encourage the development of processes and equipment that will avoid the wasteful use of energy and that will minimize harm to the environment;

(b) to explore for, produce, manufacture, buy, transport, refine, sell and otherwise acquire, develop and deal in hydrocarbons and other forms of fuel and energy;

(c) to subscribe for, purchase, take in exchange or in payment or otherwise acquire, hold and own securities of any other person, firm or corporation having objects altogether or in part similar to those of the Corporation or carrying on any business capable of being conducted so as directly or indirectly to benefit the Corporation;

(d) to carry on any other trade or business that can be carried on advantageously as ancillary to the carrying out of the objects of the Corporation set out in clauses (a), (b), and (c); and

(e) to guarantee, with or without security, the performance of contracts and the performance of the obligations or undertakings of any person, firm, or corporation, including the payment of dividends, interest, principal and premium, if any, of or on any securities, mortgages or liabilities of any such person, firm or corporation. 1974, c. 101, s. 6.

This statement is extensive and might, at first, appear to give adequate direction to the corporation. Several problems are, however, on reflection, apparent. Firstly, these objectives are set by the Ontario Legislature, a body which, as we have already seen, is only marginally involved in ongoing monitoring of corporation performance. Thus, if clarification is required, a Minister or Cabinet or lesser civil servants will have to interpret the Legislature's intent and pass it on to corporate management (as we shall shortly see, usually in less than satisfactory ways). Thus information Costs (interpretation and error Costs) are incurred.

Secondly, the "mandate" is framed in the most general terms and yields little insight into the true priorities of the shareholder. For example, with limited funds, should the corporation concentrate on developing solar energy or alternative sources of petroleum? Should it focus on developing new energy sources or conserving current sources? To what level of risk should the corporation invest in exploration of potential new oil fields? In other words, what trade-offs should be made? Again, interpretation and error Costs are involved, Costs which would not be present in the private sector not because trade-offs need not be made there, but because the parameters (i.e. maximizing profits) are known.[265]

These problems are exacerbated in the many cases of Crown corporations which have not received as detailed a statutory mandate as the O.E.C. For example, the closest reference to corporate objectives found in the Air Canada Act, 1977[266] is found in s.7(2) (subtitled "Business Principles") which states:

> In discharging its responsibilities under this Act, the Board shall have due regard to sound business principles, and in particular the contemplation of profit.

This not only amounts to little more than a mandate to "go forward and be good businessmen"; it also suggests that the main objective of the company is to maximize the bottom line rather than to achieve other objectives of public policy.

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[65] That is, in neither private nor public sector can one eliminate the costs associated with uncertainty and risk. The Costs described here arise over and above those inherent in doing business.

[66] Supra., n. 46.

Finally, as mentioned in the first section of Chapter II, not all Crown corporations have evolved through Parliament or the Legislature; the C.B.C.A. (and equivalent provincial legislation) makes no reference to Other Policy Objectives.

Thus, in nearly all cases, the constituent Act (if it exists) does not adequately set out the corporation's mandate and high information, interpretation and error Costs are incurred.

2) Corporate Plans

Some commentators on Crown corporations have emphasized the potential utility of a corporate plan in specifying Other Policy Objectives[267] and several jurisdictions have instituted such a concept.

At the federal level, section 129 of Bill C-24 requires that each "parent Crown corporation" annually submit a corporate plan to the appropriate Minister for the approval of Cabinet and, if required under the Regulations, that of the Minister of Finance; in practice, the latter's input is always required if the plan contemplates corporate borrowing. The statute goes on to set out certain content and form requirements for the plan (s.129(3) and (4)) and limits corporate activity to business consistent therewith (s.129(5)).

One might, at first, expect that although this process clearly differs from the private sector (where corporate plans do not go to shareholders at all), it is well-justified in terms of meeting concerns for objective specification. Indeed, as the process has only been implemented within the past six months, we may eventually find that this is the case.

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[67] See, e.g., Trebilcock, supra., n. 16.

Several potential problems, however, emerge even at this early juncture. Firstly, it appears that many corporations had instituted the corporate plan procedure before Bill C-24 was promulgated (for example, Air Canada). There was no indication during interviews that apart from the extension of the plan's time horizon (from three to five years in the case of Air Canada), any substantial changes in content will now be effected. Thus, any problems which existed before may well still persist.

Secondly, the corporate plan procedure is not generally confined to specification of the corporate mandate. For example, the first year of the plan usually coincides with that year's capital budget. While it is likely quite expedient and "efficient" to approve the two in tandem, there is at least some risk that the "hard numbers" of the budget will attract government's attention over the more "ephemeral" corporate objectives. Thus, the plan may accomplish little more than that which is achieved when the budget is approved.

Thirdly, it appears that corporate plans have often not been fully approved at the federal level until after the fiscal year to which they relate has commenced.[268] Whether or not this practice will change owing to the now compulsory Bill C-24 procedures remains to be seen.

Finally, one must look askance at the sheer mass of resources which go into preparation of a corporate plan requiring all of the particulars specified in s.129, in addition, to the summary required under the Act.

Saskatchewan has also instituted a strategic plan concept. The ten-year plans are prepared by the corporations in regular consultation with the Crown

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[68] Supra., text accompanying n. 239.

Management Board and need only receive the blessing of that body. They include a "Mission Statement" (which must receive Cabinet approval) as well as a one-year "profit plan".

In addition to problems analogous to those the federal system already detailed, one must query the value of a ten-year plan, since corporate officers across the country generally seemed to agree that, at best, predictions beyond three years are worth little and, further, that any change of government within the ten-year horizon (likely to occur at least once) will render the plan "useless".

Further, there is some indication that unless the Premier himself passes upon the Mission Statement, the corporations are unlikely to take its terms of reference as seriously as would ideally be the case.

Thirdly, the corporations indicate that, in practice, their objectives are communicated to them, if at all, by the Minister who sits on the Board and now via the plan.

Finally, the C.M.B. itself indicates that its primary concern is with profit. If so, then one must query the effectiveness of the plans in specifying Other Policy Objectives.

The province of Quebec has also instituted a corporate plan instrument, called a "plan de developpement".

The Hydro Quebec plan is quite extensive, setting out the corporation's objectives and strategies on a three-year horizon and including a ten-year "energy resources framework". It is submitted to the responsible Minister as well as a Parliamentary Commission. It is not clear, however, whether any of these bodies actually have to "approve" the plan; apparently this has never been done in writing and no plan has even been rejected nor had changes made to it.

A plan de developpement is also required under Section 26 of the Soquem Act.[269] The Act states that the government will set guidelines for its format, but this, apparently, has never been done. Further, the first plan prepared took some 13 months to review (by the responsible Minister and Cabinet); the second was submitted in July, 1982 and remains unapproved.

None of Ontario, British Columbia or Nova Scotia require the submission of corporate plans, although many corporations in B.C. have agreed under their Fiscal Agency Agreements to submit five-year plans to the Minister of Finance "for information purposes".[270]

In Ontario, however, the above-noted Memorandum of Understanding provides a potential vehicle for government to establish the corporate mandate. In fact, the very "purpose of such a memorandum of understanding is to set out the objectives, priorities and performance expectations of the [Crown corporation] . . . ."[271]

The stated intent fits perfectly within the framework suggested by this study. Unfortunately, however, the body of the Memorandum may not meet such expectations. For example, Article 2 of the O.E.C. Memo, entitled "Objects

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[69] L.R.Q. 1977, c. 5-19.

[70] Treasury Board Report, supra., n. 11, at p. 8. See, e.g., the B.C. Rail Memorandum, supra., n. 234, s. 4.1.

[71] O.E.C. Memorandum, supra., n. 236, Recitals at p. 2.

and Powers of the Ontario Energy Corporation" simply reiterates the language of s.6 of the O.E.C. Act, set out above.[272]

Thus, the corporate plan and related objective-specification instruments used in the different jurisdictions exhibit similar pitfalls: they run for periods longer than would be the case in private enterprise, sometimes require several layers of shareholder approval and may add little in the way of clarifying objectives. Interpretation, error and information Costs remain high.

3) Government Directives

The government directive provides an important potential vehicle for advising Crown corporations of government policy priorities. It is available in most jurisdictions.[273]

The one example of the use of this instrument uncovered during the course of my interviews concerned directives issued to Ontario Hydro with regard to wage restraints. On the assumption that such directive ties directly in with the government's policy of fiscal restraint, this would appear to be an ideal use of the vehicle to communicate policy objectives clearly, simply and accurately.

Unfortunately, however, it is not used with any degree of regularity. This is sad, but not surprising, for our economic model of representative democracy predicts that politicians will have the incentive to remain as "independent" as possible from public enterprise and to commit themselves as rarely

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[72] Supra., text accompanying n. 265.

[73] See, e.g., Soquem Act, supra., n. 269, s.23; Bill C-24, supra., n. 12, s.99.

as possible to paper, for fear of being "tainted" by any "scandal" which may touch the corporation.

4) Other Methods

How then are objectives communicated to Canadian Crown corporations? The answer is by and large, "unofficially", through various channels.

By far, the most prevalent is through the responsible Minister who either sits on the Board (e.g. Saskatchewan) or otherwise maintains close contact with corporate management (e.g. Quebec). It is, obviously, difficult to measure how effective a technique this is. Parties interviewed uniformly agreed that the answer depends in large part on the personalities of the particular Minister and the board of directors; the former will change at least once every few years, whether or not there is a change of government.

In addition, I was advised that some senior corporate officer look to Cabinet Minutes or speeches made by the responsible Minister or other Cabinet Ministers for the government's general policy direction.

Finally, some individuals interviewed felt that real evidence as to Other Policy Objectives came only from the Premier or Prime Minister himself; policy thrust was determined from listening to political speeches and divining the implications for the corporation in question. Senior officers and board members could thus develop "a feel for what is important" and for "which issues are politically sensitive". As suggested by one senior officer interviewed, "The situation is one of ex post facto policy development and the King changes every four years."

Thus, there is no discernible evidence that the above noted concerns of the Wolff Commission are adequately met in any of the jurisdictions under discussion. This problem is perhaps best illustrated by the fact that despite the various official and unofficial channels for communicating Other Policy Objectives, several corporations (e.g. the O.E.C. and B.C. Rail) have developed Director's Handbooks to clarify for internal use what are otherwise regarded as uncertain mandates; the irony (if one can call it that) is that, in many cases, this document has never been approved (not perhaps, even seen) by the government.

This chapter has, therefore, identified a plethora of Costs incurred due to inadequate specification of corporate objectives above and beyond those which must necessarily be incurred:

A) interpretation Costs (by directors, managers and possibly Ministers/Cabinet interpreting legislation),

B) error Costs (same),

C) duplication of effort (corporate plans, summaries, capital budgets, breakfast with the Minister), and

D) layering Costs (having several different bodies involved in communicating objectives/approving items such as corporate plans).

Moreover, there has been concern that the mandates of a number of Crown corporations overlap either with those of other corporations or of Departments or Ministries. For example, both the Memorandum of Understanding for Ontario Hydro and the description provided in the Estimates for the Ministry of Energy's Energy Conservation Program focus on conservation and the efficient use of energy resources.[274] Similarly, the Wolff Commission documents S.E.D.C.O. management as stating that that company has a major role to play in attracting new

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[74] *Treasury Board Reports*, *supra.*, n. 11. at p. 35.

industry to Saskatchewan while, at the same time, the C.I.C. and the Department of Industry and Commerce considered this task to fall within the latter's assumed responsibility.[275]

Finally, we return for a moment to the notion of profit -- the objective which, on our initial premise, is insufficient to support the existence of public enterprise, but which is also both the cheapest and most accessible index of firm performance and likely the key manner in which managers (and perhaps government monitors) achieve "prestige".

During interviews, officials at both corporate and government levels were anxious to impress that Canadian Crown corporations were profitable, or, at least, tried hard to be so. Such evidence is buttressed by the approach taken in s.7(2) of the Air Canada Act, 1977 (above), and by statements such as the following submission by the C.N.R. to the MacDonald Commission:

> From the outset, C.N.'s mandate has been to provide transportation services on a commercial basis. This means operating efficiently and reliably, making a profit and financing our own operations and expansion. Some may feel that a Crown Corporation's concern with social responsibilities should be greater than one would expect from a good citizen in the private sector. This is not our view.[276]

If this, indeed, represents the general view of Crown corporation monitors, then the error Costs involved in monitoring Other Policy Objectives may be even larger than at first imagined.

This is not to suggest that profit is "bad", but merely that it is, perhaps, in the public sector used as shorthand for "efficiency" (which clearly is "good"). That is, if public enterprise is focusing on profit (i.e. wearing

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[75] Wolff Commission Report, supra., n. 1. at p. 5.

[76] Canadian National Railways Company, "A Comment on the Role of Crown corporations in the Canadian Economy" Submission to the Royal Commission on the Economic Union and Development, November, 1983.

Private Sector Glasses), it may well be ignoring Other Policy Objectives, without which the argument in favour of having public enterprise in the first place loses its foundation.[277]

b) Financing Costs

Crown corporations recognize distinct Advantages in financing their operations, as government generally either finances them directly (via appropriations from the Consolidated Revenue Fund or by issuing debt in the open market) or guarantees their loans. Even in cases where a government guarantee does not stand behind corporate debt (e.g. Hydro-Quebec), many corporate officers expect that they receive top ratings in the capital market (generally, "Triple A") as the market "knows that government is behind them."[278]

Thus, the Cost of money to Crown corporations is usually below that of comparable private sector firms and below what their financial performance and capitalization[279] would otherwise predict; it represents perhaps the most important Advantage which accrues to public enterprise in Canada.

There are, also however, certain Costs incurred in financing which, to a greater or lesser extent, may offset this Advantage, namely the extra administrative and transaction Costs accrue as a result of the mass of approvals which the Crown corporation must receive and procedures which it must adhere

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[77] Unless, of course, one's political philosophy holds that all wealth should be nationalized.

[78] One exception is Air Canada which advised me that they borrow at a slightly higher rate than the federal government.

[79] Crown corporations tend to be very highly levered and would, absent the public Shareholder, anticipate a relatively high cost of debt capital. See G. Schwantje, letter to D. Gracey, July 17, 1984 (Ottawa: unpublished, 1984).

to prior to issuing the bonds. For example, under s.2 of the British Columbia Railway Finance Act,[280] that company may borrow funds if it obtains Cabinet approval and stays within a $1.2 billion ceiling (s.14 of the Act). Ostensibly, these are the only restrictions. However, under its Fiscal Agency Agreement, the company may not even enter negotiations with an investment banker or an underwriter without the Minister's consent (s.6.1). Further, the Minister chooses the underwriter (s.6.3) and may carry out the negotiation on the corporation's behalf (s.62). Even lines of credit at the bank must be negotiated jointly by the corporation and the Minister (s.7.3) and the corporation must "consider" tendering for banking services every five years

(s.7.4.). On top of these, the company must pay the fiscal agent (the Minister of Finance) a fee for his services equal to 1/3 of one per cent of the principle amount of the issue (s.11.1 and s.6.0 of Appendix A).

Similar transaction Costs may be incurred when the corporation is funded directly by the government. For example, the Ontario Energy Corporation was at one point "guaranteed" funding of $23 million per year for each of five years, but had nonetheless to go back to government in each year to justify the appropriation, seemingly deadweight Cost.

Yet another Cost is implicit in the fact that Crown corporations tend to be very highly levered;[281] there is, presumably, only so much more debt that they can raise on the open market. As they obviously cannot issue more equity (unless the government decides partially to privatize), access to outside funds is limited.

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[80] R.S.B.C. 1979, c. 39.

[81] Schwantje, supra., n. 279.

Whether or not these Costs are offset by the above-noted Advantage of being able to obtain "cheap money" requires an empirical analysis which lies beyond the scope of this paper; it also is not the point. The high credit rating of Crown corporations may be perfectly justifiable on the same basis as that of any company with a high credit rating: that is, they are, by their very nature, low risk ventures and the capital market assigns a premium to that fact. To suggest that any Costs are "offset" by lower interest payments merely conceals the fact that a cost-efficient Crown corporation might realize both the Advantage of "cheap" money and lower transaction Costs than currently exist. Thus, the Costs remain ones which must be justified by Other Policy Objectives.

1) Dividends

As a general rule, Canadian Crown corporations have been grossly deficient in paying dividends to their shareholder. For example, the Crown corporation sector in Saskatchewan reported, in the aggregate, more than $650 million in profits during the seven-year period ended March 31, 1982 but paid out dividends of only $145 million.[282]

This is in no way to castigate the corporations, for the consensus of opinion among senior corporate officers interviewed clearly is that, at least until recently, there has been very little (if any) pressure placed upon them by government to return profit to government coffers. Rather, as one officer told me, "They have a [government] Department mentality. They think that

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[82] Wolff Commission Report, supra., n. 1, at p. 12.

the money they give us is free. They don't expect a return and are happy as long as we don't come back for more".

Such philosophy generates several Costs. One is first led to query the incentive structure facing managers who are not obliged to provide any (let alone a maximum) rate of return to the shareholder; even the best of souls might not put his or her all into ensuring productively-efficient operations.

Secondly, the absence of pressure to pay dividends results in even "cheaper" money than the previous subsection would predict: debt is "cheap" and equity is virtually free. Where as we found the former to be justifiable by virtue of the low risk associated with public enterprise, the latter represents an artificially low cost of money, decreasing its opportunity cost to the corporation and, if economic theory is correct, thereby inducing an inefficient allocation of funds, wholly unrelated to Other Policy Objectives.

Moreover, non-payment of dividends bears a direct relationship to the firm's retained earnings account which, in turn, can be utilized to finance projects whose costs then become "hidden" from the government shareholder. Indeed, the preceding discussion suggested that both managers and politicians would have an incentive to attempt to finance out of surplus, the former in order to stay as independent from government as possible, and the latter in order to stay out of the Departmental/Ministerial budget, Consolidated Revenue Fund or appropriate Policy Envelope. The absence of pressure to pay dividends therefore contributes substantially to "Hidden Costs".

All of these Costs become all the more impressive when one recalls that Crown corporations tend to have very high debt/equity ratios. In theory, the higher the leverage, the greater the risk of equity capital, the greater the return which the "rational" equity owner would demand.[283] If anything, then, the shareholder of Crown corporations should be demanding a higher, rather than a lower rate of return to its investment.[284] We, thus, find yet another hidden subsidy to Crown corporations, analogous to the tax immunities described in an earlier section.

Before concluding, we would note that the federal government has, in some cases, instituted a 20% dividend policy, for example, for Teleglobe Canada, Air Canada and Canadian National Railways. Similarly, the Quebec government has, at least in the case of Hydro-Quebec, legislated a dividend 75% of "surplus" and Sask Tel advises that it regularly pays one-half of "profits" out in dividends. While such measures should help ensure that management face more accurate market signals and help return funds to the Consolidated Revenue Fund for use in other projects, it is difficult to determine how the relevant figures were arrived at. Indeed, there is evidence that at least one company's dividend rate will jump very substantially in the next few months, suggesting that it has been far too low in the past. Further, in at least one instance, I was advised that the dividend policy then in place was suggested not by the government, but by the company's board of directors (on consultation with

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[83] I will not here attempt to summarize the debate generalized by the Modigliani-Miller hypothesis that the overall cost of capital to the firm remains constant no matter what the debt equity ratio, and their corollary that the return to equity actually decrease as debt rises. For a more extensive commentary on the hypothesis and the suggestion that the overall cost of capital may remain constant as leverage increases (i.e. supporting the M-M hypothesis) despite an increase in Ke as the firm becomes more levered, See Van Horne, *Financial Management and Policy*, in Brudney and Chicelstein, *supra.*, n. 257, at pp. 393-405.

[84] Note that Hydro Quebec claims to have a return on equity of 13-23% which, they claim is very satisfactory in the industry. This, of course, is not adjusted for Advantages.

the appropriate Minister). While this would also be the case in the private sector, one must remember that the latter is subject to the threat of private shareholders selling out if dividends are unsatisfactory, i.e. it is effectively constrained by the fact that property rights are readily transferable. Without such constraint, it is difficult to determine what factors motivated the choice of the 20% or 75% or 50% yields.

Thus, although the institution of such dividend policies clearly represent a move in the right direction, substantial Costs may still persist.

d) Corporate Authority

1) Creating Subsidiaries

Many of the limitations on the authority of Canadian Crown corporations to conduct businesses in the same manner as private enterprise have already been canvassed in other contexts above. Foremost among these are the requirements for various levels of government to approve corporate borrowing, capital budgets, corporate plans and the selection and remuneration of the Chief Executive Officer.

In addition, the following points should be noted. Crown corporations in most jurisdictions (except federally[285]) may, in law, create subsidiaries without governmental sanction, but, in practice, Cabinet approval is usually sought,[286] another Cost to the corporation. This is not to suggest that approval should not be required in the public sector; indeed this is perhaps a prime example of where the balance between managerial flexibility and monitoring

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[85] Bill C-24, supra., n. 12, s.101.

[86] Treasury Board Report, supra., n. 11.

of corporate performance of Other Policy Objectives should be struck in favour of the former. We return to this issue in Chapter V.

2. Winding up

Government approval (usually by Cabinet) is required in all jurisdictions in order to wind up or dissolve a Crown corporation. This is no different from private enterprise where a special resolution of (each class of) shareholders is generally required (e.g. C.B.C.A., s.203) and no Differences are apparent so far.

Note should be made here, however, of Ontario's Sunset Review process, designed to focus government's attention on whether or not the original program represented by the Crown corporation in question is still relevant, i.e. on whether the use of public enterprise still satisfies the calculus of instrument choice.

Few Reviews have been completed so far, but they constitute a potentially costly process.

The Review is prepared by the responsible Ministry in consultation with the corporation and other Ministries "as required". Once the Minister has attached his or her recommendation to the Review, it goes to Management Board and the appropriate Policy Field Committee of Cabinet (composed of Ministers) for discussion. That recommendation is then put before Cabinet for approval and is, finally, tabled in the Legislature. The decision to terminate or continue the corporation is made by way of Order-in-Council or legislation.287 If the decision is to continue, a date will be set for the next examination, approximately 5 years hence.

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[87] Ibid., at p. 34.

Sunset Review is mandatory for all Ontario agencies created since March 1980 and is gradually being phased in for older corporations. To date, no Schedule II corporation has been reviewed, but IDEA Corporation will soon be subject to the process.

Clearly, the Review is not conducted by private enterprise; hence, another Cost arises. As in the case of creating subsidiaries, however, it (or at least the concept of regular review) may be quite justifiable in terms of Other Policy Objectives.

One further point to note in this context. In some cases, a government does not bother to dissolve a Crown corporation but leaves it "on the books" even though its activities have ceased (for example, Clairtone Holdings in Nova Scotia[288]). The additional Cost of so doing (i.e. the administrative Costs of reporting on the company to the Legislature within the Public Accounts each year) are not high, but are extraneous.

3) Corporate Decisions

Many Crown corporations are, in their empowering legislation, endowed with all the "capacity and power of a natural person", much as is a privately-owned company, and their boards are statutorily given responsibility for the "management of the businesses, activities and other affairs of the corporation" (e.g. s.118 of Bill C-24). Despite this ostensible freedom, management's behavior is nonetheless then constrained by the various approval schemes already described and by the obligation to not depart from corporate or strategic plans without ministerial approval (e.g. s.8.5 of the O.E.C. Memorandum; s.129(5) of Bill C-24).

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[88] Ibid., at p. 52.

As we have already seen, many Crown utility corporations are not free to set prices of their products nor to expand manufacturing capacity, due to the requirement of regulatory, often in addition to ministerial, approval; as this is equally true for privately-owned utilities, we do not identify this as an important Difference. In the case of Crown corporations, however, the interference with operations decisions may go so far as to have, for example, entities such as the Public Accounts Committee examining construction and repair programs[289]; this clearly diverges from the private sector benchmark.

Private corporations are free to invest corporate surplus as they see fit, subject only to shareholders' approval or disapproval of the ultimate bottom line and share prices. Not so in the case of Crown corporations, many of which can invest only in Canada Savings Bonds (a far more stringent restriction than that applied to banks or trust companies) (e.g. Teleglobe Canada) or can have investment undertaken only by their responsible Minister who then reports back to the company on it (B.C. Rail Memorandum, s. 8.3.).

Similarly, Crown corporations cannot generally diversify their operations without Cabinet approval, not necessarily because such diversification might not meet an Other Policy Objective, but because other participants in the new market may see the Crown corporation as having "unfair Advantages" (i.e. tax immunities, government funding or credit ratings). Thus, the

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[89] Internal material supplied by the Economic Council of Canada. Another example is B.C. Rail which must, if it plans to build an "uneconomic rail line", first consult at the technical level with the Technical Committee, composes of B.C. Rail employees and civil servants. The Steering Committee (composed of several Deputy Minisiters) is then involved, although their approval may, in practice, be more of a "rubber stamp" than true review. The decision then goes to the full Cabinet or the Economic Committee of Cabinet, and finally, to Treasury Board which may, right at the end of this extensive process, veto the plan on financial grounds.

issue becomes "politically sensitive" and restraints on corporate activity are introduced.

The lack of management's authority may extend to all "major decisions" of Crown corporations, whether or not approval mechanisms are explicitly ensconced in legislation, particularly (as volunteered by nearly every corporate officer interviewed) when the decisions in question are deemed by the company's board to be "politically sensitive". The situation may be worst in the case of the four corporations which the federal government of Canada hopes to privatize: major decisions, for example, of Canadair must now go to the corporation's own board, the Canadian Development Investment Corporation ("C.D.I.C."),290 the C.D.I.C. Board, the Department of Finance, the Treasury Board, the Department of Regional Industrial Expansion ("D.R.I.E.") and possibly even Cabinet; the hard Cost of such a series of approval was estimated for me at $2 million, and the company is hamstrung throughout the process.

The Canadair example may be somewhat extreme, but it is not as much so as one might hope. Many individuals interviewed suggested that excellent business opportunities go by because no government official is willing to identify him- or herself with the downside of a business risk and/or because the delay involved in obtaining a decision, in fact, determines it: the opportunity simply disappears before a final decision is reached. One senior officer suggested that certain opportunities just don't present themselves at all because the private sector shies away from the high Costs of dealing with

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[90] The government corporation currently holding the shares.

government bureaucracy.[291] This is perfectly consistent with the model of political behavior developed above and, in fact, is quite rational from the politician's point of view: why accept the downside of a decision when you will likely not benefit from the upside?[292] Unfortunately, the Costs involved may be extremely high.

The lack of flexibility and managerial discretion which we are uncovering here obviously carries with it a fair degree of frustration for corporate management. More important in our context, it likely reduces the supply of public sector managers and stimulates the incentive of those in it not to monitor Other Policy Objectives, as we would hope, but to find ways to bypass the government shareholder as often as possible.[293] This further intensifies the high information and monitoring Costs which we have already found to exist in the sector.

Finally, the fact is that with management frustrated and facing high negotiation Costs, individuals with less than optimal expertise may end up making the decision. To cite yet another Canadair example, it was suggested to me in an interview that the approximately $1.4 billion losses recently suffered were due primarily to the fact that the Challenger was developed with an engine that had never been tested before. It was not clear who had

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[91] It would be interesting to study this effect specifically in the context of government investment companies which joint venture with the private sector (e.g. Soquem).

[92] Unless voters are particularly cognizant of and place great importance on the upside; this is very unlikely in the case of, e.g., a corporate purchase of a particular building.

[93] No slight on management is intended here. The point is that, given the current institutional infrastructure, this is perfectly rational behavior.

made the decision to do so; it was clear that no privately-owned aircraft company would ever take such an unwarranted risk.

Thus, the Costs associated with lack of adequate corporate authority in the Crown sector may be quite serious.

e) Other Differences

In the course of conducting interviews and research, several other Differences from private enterprise were brought to light. Briefly (I promise), they are as follows.

1) Customer Relations

There is a Cost associated with the very fact that the Crown corporation is sometimes seen by the public as being a direct arm of the government. For example, the C.E.O. of one public utility told me that a customer wrote directly to the Premier's office asking to have his service disconnected while he was out of town. The inquiry was then referred not to a clerk in the Consumer Service Department (as would be the case in the private sector) but to the Crown corporation's president.

2) Information

In a related vein, corporate officers across the country report that much of their time and energy is spent answering inquiries from the Premier/Prime Minister's office or other members of the Legislature. This involves a Cost not only of time spent by senior officers in handling this sort of matter when lower-level individuals could easily do so, but also of adding to the already high frustration level of top management and lowering incentives to enter the public managerial labour market to monitor performance once there.

A similar Cost arises in situations where the Crown corporation is seen, in addition to its other Objectives, as a "yardstick" of market activity.[294] For example, the O.E.C. is expected, pursuant to its Memorandum of Understanding, to "share . . . knowledge and perceptions [of the overall energy environment] in a timely way with the Minister" (s.6.1), and provide him on an ongoing basis with information relating to "the energy environment, the government's energy policies or the strategies and programs of the Minister of Energy" (s.6.3). Such process can be very Costly, albeit justifiable in terms of Other Policy Objectives.

3) The Corporation as a Statutory Creature

Several institutional Differences are associated with the fact that most Crown corporations are created pursuant to their own constituent acts.

We have already seen that amendments to the corporate charter must be made by statute, rather than simply by filing Articles of Amendment. In addition, certain corporate decisions become statutorily mandated. For example, rates for the Autoplan business of the Insurance Company of British Columbia ("I.C.B.C.") are set by the Cabinet as Regulations to the *Insurance Motor Vehicle Act*. Thus, changes do not simply require amendment of a standard form contract, but, rather, must be drafted by a Legislative Council and pass through the appropriate channels as amended regulations. The insurance policy

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[94] See Chapter IV, *infra.*

is, consequently, rarely changed more than once per year. The Costs involve extra time, delay and loss of corporate flexibility.

4) Buying Canadian

Another Difference commonly cited by corporations involves the implicit government policy to "Buy Canadian" or, even more specifically, to "Buy Saskatchewan", or whatever. While many large corporations, as "good corporate citizens" would likely do the same, there is here the added pressure of, for example, a Canadian traveler who may complain to his M.P. if Air Canada does not serve Canadian wines.

5) Public Scrutiny

This example, along with the example of the ratepayer who called the Premier illustrates the major Difference associated with the fact that Crown corporations are highly visible and "belong to the taxpayer". True, all public utilities (whether privately- or publicly-owned) are subject to a high degree of media coverage and public scrutiny. However, the problem (and the Cost) is exacerbated when the public views the corporation as "its own": "I'm paying for this company and I will complain to my M.P. if I don't get the service I want". The M.P. concerned with voter maximization (and, as one C.E.O. put it, with the "cost of political pride"), feels obliged to follow up on the complaint directly to the president's office, which office will surely be open to him. The Cost here may be quite high; corporate officers interviewed estimated that between 20% and 80% of their time was spent on what I shall broadly call "Public Relations" work and some corporations specially designate staff to handle legislative inquiries. This is a particularly important Cost to keep in mind in completing the calculus of instrumental choice.

6) Government Administrative Practices

Crown corporations are often subject to procedures which have been developed for the administration of government in general. For example, s. 14.4 of the O.E.C. Memorandum requires that, as "appropriate", the company "follow and adopt internal administrative procedures and guidelines modeled on those of the government [and based] on the principles inherent in the Public Services Act, Regulations thereunder and the Government's Manual of Administration. . . ." The B.C. Rail Memorandum, it will be recalled, requires that the company "consider" tendering for bank accounts every five years and a Saskatchewan corporation advised that, although free to make its own purchases, it must do so following the government process blueprint.

These requirements all entail Costs which are extremely difficult to assess, for many (as in the B.C. Rail example) are "informal" and others are not requirements at all but simply things which corporate management "just knows" (for example, the "requirement" to "Buy Canadian" or to use known government suppliers).

IV. Other Policy Objectives

The preceding Chapters deciphered many Differences between the operations of the Canadian Crown corporation and the representative private sector corporation. Some of these -- Costs - involve extra costs incurred by the public enterprise or its government shareholder in or due to monitoring corporate performance, interpreting corporate objectives, reducing managerial flexibility and inadequate or inaccurate incentives of both government and managers. Others -- Advantages -- related to specific privileges endowed upon Crown agents (primarily tax immunities and low costs of capital) and represented subsidies by the Canadian taxpayer or private individuals to the public firm. It was the original premise of this paper that the principle of productive efficiency demands that all such Differences be justifiable -- "matched" -- by one or more policy objectives other than the attainment of profit or be eliminated.

This chapter will, accordingly, describe a broad range of Other Policy Objectives, gleaned both from the literature[295] and interviews conducted for this research, against which, in Chapter V, the Differences will be assessed.

a) Nation Building

Probably the most oft-cited rationale for public enterprise in the Canadian context is that of national and regional development, the unification of the

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[95] Far more extensive discussions of each of the following, see, for example, E. Kirsch and J. Yall, "Crown Corporations" (unpublished paper, Univ of Toronto Faculty of Law, Sept., 1979); Trebilcock and Prichard, supra., n. 6, at pp. 39-74; A. Tupper, "The Nation's Businesses: Canadian Concepts of Public Enterprise" (unpublished Ph.D. Thesis, Dept. of Political Studies, Queen's Univ., Nov., 1971); Trebilcock, supra., n. 16, at pp. 6-14; Gracey, supra., n. 228.

country along an east/west axis instead of the more natural north-south pull.[296] As stated by Professor Innis in the following well-known passage:

> Government ownership in Canada is, fundamentally a phenomenon peculiar to a new country, and an effective weapon by which the government has been able to bring together the retarded development and the possession of vast natural resources. . . . and a market favourable to the purchasing of raw materials. It was essentially a clumsy, awkward means of attaining the investment of tremendous sums of capital, but it was the only means of accomplishing the risk and of retaining a substantial share of the returns from virgin natural resources.[297]

This rationale, in fact, comprises two distinct Other Policy Objectives:

i) the goal of developing and integrating the country, or some region thereof, when market signals are such that private investors are unwilling to make certain kinds of investments or take certain kinds of risks ("Development"); and

ii) the desire to develop a national identify or preserve Canadian (or provincial) control over certain sectors of the economy in the face of pending foreign investment ("Nationalism")

The former, in turn, reflects at least three separate instances of market failure: underinvestment by the private sector due to the existence of positive externalities (social benefits) which exceed private benefits (i.e. inter-industry benefits which do not accrue to private investor, underinvestment due to imperfect capital markets, and an unwillingness of the private sector to invest in "infant industries" which, in time, might become self-sustaining. In addition, the Development Objective describes situations where the government

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[96] *Supra.*, n. 194, at p. 96, *per* Tom Axworthy.

[97] Innis, *The Problems of Staple Production in Canada* (Toronto: Ryerson Press, 133) at pp. 80-81. Note that in the last chapter of this paper, we will take issue with the last sentence of Prof. Innis' otherwise valuable statement.

has, for social rather than economic reasons, concluded that certain uneconomic activity (like providing low-cost electricity to all citizens regardless of marginal cost) is warranted.

There are numerous examples in the Canadian context of each of these. For example, the hydro-electric provincial utilities were, generally, brought into the public sector both to encourage development of other industries in the province and to ensure, as a matter of policy, that all residents of the province received low-cost (cross-subsidized) reliable service, no matter how remote their homes. Similarly, the western public sector insurance companies had as at least one original motivation the provision of coverage for otherwise uninsurable risks.

The infant industries Development Objective is perhaps best recognizable in the government's commitments to develop the oil and gas industries in western Canada (Trans-Canada Pipelines)[298], to create a transnational airline service and to build a nuclear reactor (the creation of Trans-Canada Airlines, later Air Canada, and of Atomic Energy of Canada Ltd. ("A.E.C.L."). This latter example also illustrates the Nationalism rationale: the only firms willing to invest in these novel, uncertain industries were foreign (generally American) and could not demonstrate Canada's commitment to control over her own destiny.[299] Analogous rationale is often put forward to justify the Canadian Broadcasting Corporation and much of the Crown enterprise in Quebec which was created when French Canada determined that it had to impede the flow of revenue out of the province and into the bank accounts of other Canadians and Americans;

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[98] Supra., n. 194, per Senator William Kelly, at p. 106.

[99] Trebilcock and Prichard, supra., n. 6, at p. 58.

I was also advised that the Ontario Energy Corporation's purchase of a major block of Suncor was at least in part motivated by the desire to ensure Ontario a voice in Canadian energy policy. Finally, both Telesat Canada and Air Canada provide examples of situations where Canada's position in international markets was thought to require a public enterprise spokesperson.

The above examples are far from exhaustive. The important point to remember in our context is that in most cases, alternative policy instruments were available to government, ranging from government subsidies, low-cost loans, tax incentives and guarantees, to regulation (as in the case of privately-owned Bell-Canada or CP Air). In each case, public enterprise was chosen, we assume, on the basis of the calculus of instrument choice.

b) Saving Failing Industries

A related Objective is the government's decision to nationalize an industry which would otherwise fail due, generally, to the ultimate Objective of Nation Building. Examples include Canadair Panco Poultry Limited in British Columbia,[300] and the Canadian National Railways which resulted from the merger of the Canadian Northern and Grand Trunk Railways, both already heavily subsidized and both in severe financial difficulty.

c) Maintaining Employment

The Objective here is straightforward: rather than use the obvious alternative of paying unemployment insurance and retraining workers in industries which either have become uneconomic and should (under the strict laws of economic

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[0] Gracey, "Public Enterprise in Canada", supra., n. 228, at p. 44.

theory) shut down, or which have become increasingly capital intensive, the government has chosen to keep unemployment down by taking over the firm (usually in a one-firm industry) and continuing to operate it.

Examples include the Cape Breton Development Corporation,[301] the B.C. Ocean Falls Corporation,[302] the continued presence of A.E.C.L.'s heavy water plant in Glace Bay, Nova Scotia, costing an estimated $117,000.00 per employee per year,[303] and the location by Eldorado Nuclear of a refinery in Blind River, Ontario, a decision which "made no business sense."[304]

d) National Monopoly Regulation

Yet another Objective which is often cited as a rationale for public enterprise is the desire to constrain the economic behavior of a natural monopolist who, under the laws of economic theory, will price high and produce low. The obvious examples include the major telephone and power utilities.

The clearest alternative to the public enterprise instrument in this context is regulation of privately-owned firms, much as is done in many other instances in Canada (e.g. Bell Canada, B.C. Tel) and throughout the United States. It should be remembered, however, that the previous chapter disclosed many instances where both of these instruments are used in tandem (e.g. Ontario Hydro, Sask Tel, Air Canada) to meet the single Policy Objective.

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[1] See Tupper, supra., n. 295 at pp. 51-52.

[2] Gracey, supra., n. 228, at p. 44.

[3] This figure was quoted to me in an interview by a reliable source.

[4] Gracey, supra., n. 197, at p. 100.

e) Yardstick Theory

There are at least three separate aspects to this Objective of public enterprise:

i) to provide government with "cheap" information regarding the performance of competitive firms in the industry;

ii) to reduce the possibility of collusion and other anti-competitive behavior by inserting a publicly-owned "hold-out" directly into the marketplace; and

iii) relatedly, to keep private firm competitors "on their toes."

The alternative policy instruments are, respectively, fuller disclosure requirements, tighter Combines legislation and subsidies or other incentives which reduce barriers to entry in the industries in question.

Probably the most often-cited example of the creation of Crown corporation to fulfill the Yardstick Objective is that of Petro-Canada,[305] most interesting in light of the fact that its incorporating legislation makes no reference to this choice:

> The purpose of this Act is to establish within the energy industries in Canada a Crown owned company with authority to explore for hydrocarbon deposits, to negotiate for and acquire petroleum and petroleum products from abroad, to ensure continuity of supply for the needs of Canada, to develop and exploit deposits of hydrocarbons within and without Canada in the interest of Canada, to carry out research and development projects in relation to hydrocarbons and other fuels and to engage in exploration for and the production, distribution, refining and marketing of fuels.[306]

Similarly situated is the Ontario Energy Corporation, whose empowering legislation does not mention the Yardstick Theory but whose Memorandum of Under-

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[5] See, for example, Trebilcock and Prichard, supra., n. 6, at pp. 69-70.

[6] Petro-Canada Act, s.c. 1974-75-76, c.61, s.3.

standing mandates the provision of market information to the responsible Minister.307

f) Security of Supply

Related to the Yardstick Objective only insofar as it tends to apply to the same Crown corporations is the Other Policy Objective of securing the supply of certain goods and services which are considered indispensible to the nation's well-being -- for example, the 1975 establishment of Petro-Canada, at least partly in response to the mid-1970's oil crisis. Other available instruments include the usual subsidies/tax incentives for exploration, conservation, etc. and some of these have, in fact, been employed in conjunction with the use of public enterprise (e.g. the Petroleum Incentive Program and the various oil and gas tax shelters programs which have existed during the past ten years).

g) National Security and Secrecy

This Objective is generally used as justification for the many Crown corporations created during W.W. II -- e.g. Polymer Corporation, created in 1942 in order to produce synthetic rubber as part of the Allied War effort and Eldorado Mining and Refining Corporation (now, Eldorado Nuclear Ltd.), acquired in the same year to supply uranium to the Manhattan Project and produce an atomic bomb.

It is difficult to propose alternative instruments which could satisfy this particular objective, for a country at war is characterized by specific

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[7] Supra., text accompanying n. 294.

security needs which few would suggest should be left to the private sector. The Objective is, however, particularly difficult to cite as justification for Differences in light of the fact that the war is 40 years over; as suggested by Borins, "The major reason for keeping Polymer [after the war] was not national security but economic viability,"[308] i.e. the company was "making money," so why privatize it.[309]

h) Monitoring Government Productivity

Sometimes, Crown corporations are created specifically to act as an official monitor of other government agencies. Examples include the B.C. Building Corporation which "charges back" services performed for the public sector and the Saskatchewan Crown Management Board, the holding company which monitors other Crown corporations in the province.

The alternatives are, obviously, other monitoring methods such as use of private sector contracts or the model proposed in Chapter V.

i) Testing Ground

It has been suggested that Crown enterprise is sometimes used as a testing ground for untried policies such as the representation of employees on corporate boards of directors.[310]

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[8] Borins, "World War II Crown Corporation: Their Functions and Their Fate", in Prichard, supra., n. 2, at p. 465. See also comments of C. D. Howe, Minister of Munitions and Supply, Canada. Parliament. Debates, (Ottowa: House of Commons, 4th session of the 19th Parliament, June 16, 1943), at p. 3707.

[9] We return to this shortly, as the "Profit Objective".

[10] Gracey, supra., n. 194, at p. 100.

It is easy to conceive of alternative instruments such as the use of consultants or research or even subsidies to the private sector to test such problems.

j) Social Policy/Externalities

The objectives of commercial Crown corporations often include social goals such as energy conservation (e.g. Ontario Hydro) and encouraging traffic safety (e.g. the Insurance Company of British Columbia), uneconomic externalities which the private sector may have no incentive to invest in.

Alternative instruments would, again, include specific incentives or subsidies.

k) Capital Markets

The rationale here involves a choice of public enterprise to provide services which the government has, for various policy reasons, determined to be compulsory. The best example is that of compulsory auto insurance, provided by the Insurance Company of British Columbia and Saskatchewan Government Insurance.

The Objective is to provide the mandated coverage at cost on the theory that that which is compelled by the state should not be profitable to the private sector. As with the Control of Natural Monopoly Objective, the most likely alternative instrument is rate regulation of a privately-owned insurance company.

l) Co-ordination

Occasionally, cheap policy co-ordination is cited as an Objective of public enterprise. This Objective is related to the Yardstick Objective above, and analogous comments apply.

m) Poor Rationales

There are several other Other Policy Objectives which are, from time to time, cited as supporting the case for public enterprise, but which, we suggest, in fact constitute poor rationales.

The "Profit Objective" was hinted at in the last sentence of Prof. Innis' above-noted quote, as well as in Borins' comments on the post-war continuation of Polymer Corporation. It is further evidenced in the philosophy held by the Rt. Hon. C.D. Howe, the "grandfather of Canadian public enterprise," as interpreted by Borins: apparently, "he had no qualms about government ownership of profitable enterprises even if no specific policy objective were being served."[311] Perhaps most importantly, it was cited by many interviewed as the primary focus of public enterprise in Canada today, as exemplified in the excerpt from the C.N.R. submission to the MacDonald Commission, quoted earlier.[312]

Such a position reflects nothing more nor less than the use of Private Enterprise Glasses in the public enterprise arena. That is, while we would certainly not suggest that public enterprise should not be cost efficient

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[11] Borins, *supra.*, n. 308 at p. 464. C. D. Howe was Minister of Munitions and Supply, Minister of Reconstruction, and finally Minister of Trade and Commerce during W.W. II and in the post-war years.

[12] *Supra.*, text accompanying n. 276.

(indeed, quite the contrary), we would emphasize that profit maximization alone cannot justify Costs or subsidized Advantages; by definition, the profit-maximizing solution is exactly what our private sector benchmark already incorporates.

Similarly faulty reasoning is applied if one attempts to cite the Objective of ensuring independence from government in and of itself as the justification for Differences. Yet this is often utiliized. As suggested by Gracey:

> The basic raison d' etre of the federal Crown corporation has been to separate the management of an activity from continuous partisan intervention and day-to-day government or parliamentary scrutiny or debate.[313]

Indeed, the simplest way for government to remain independent is simply to do so, i.e. to stay out of the market. The same reasoning applies to the possible "Objective" of using an instrument which allows for flexibility, reversibility, and relatively simple (and hidden) marginal adjustments in policy; this is an *attribute* of public enterprise which may validly enter the calculus of instrument choice but is not an adequate rationale to support Costs and Advantages. Indeed, as we have earlier suggested, it *constitutes* a Cost and must itself be matched against an Other Policy Objective.

One final possible support for public enterprise which has been noted is the very desire of a government to benefit from the Advantages which accrue to Crown corporations. Perhaps the best example is the nationalization of the B.C. Electric Company following the following comments by the Premier:

> [In 1959,] I stated British Columbia's feeling that the income-tax on privately-owned public utilities should either be abolished or the

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[13] Gracey, *supra.*, n. 228, at p. 28.

> province should get 100% of such tax....I stated further that unless the Federal Government [did so], British Columbia would have to take over the B.C. Electric Company.314

The reasoning here, again, is circular: one would be citing obtaining an Advantage as the justification for incurring Costs and obtaining Advantages.

V. Rationalizing the Differences

At a recent Symposium, Don Gracey made the following comments regarding Canadian Crown corporations:

> Government loaded...down [Crown corporations] with all kinds of social and non-commercial public policy objectives. It used Crown corporations as a supposedly costless instrument to achieve social policy objectives and in a way that hid or obscured effective accountability or the disclosure of costs and results to the parliament and to the public.[315]

In a similar vein, Palmer, Quinn and Resendes, in their excellent case study of Gray Coach Lines, stated:

> We would be very surprised...if Metro taxpayers would support the present goals of [Gray Coach] if they realized the opportunity costs of these goals...Our concern is that the voting constituencies be made aware of the existence of this problem so that other more direct options for subsidization become politically feasible.[316]

As the preceding Chapters of this paper have demonstrated, Gracey is, no doubt, correct: there are clearly numerous "hidden costs" associated with the public enterprise instrument. Does this mean, as Palmer, Quinn and Resendes implicitly suggest, that the calculus of instrument choice need be revisited?

Not necessarily. That is, the calculus of instrument choice should be reviewed regularly, not because of the hidden costs, but because that is what good government is all about, and the hidden costs should be implicit in each such calculation. Whether or not this is in fact done is, of course, another matter entirely and may form a good subject for future research. For the present, we keep the two issues -- performing the calculus and (assuming that it has come out in favour of using the public enterprise instrument) determining

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[15] Gracey, supra., n. 194, at p. 37.

[16] Palmer, Quinn and Resendes, supra., n. 10., at pp. 433-434.

whether or not the identified Costs and Advantages should be eliminated from the formula -- quite distinct, and focus only on the latter.

a) Costs of Creation

The Differences in this area stem from the fact that creating Crown corporations by means of separate, non-standardized empowering statutes entails Costs of developing, amending and interpreting each piece of legislation on an individual basis.

Arguably, such Costs are justifiable both in terms of ensuring that legislators address themselves to the specific Other Policy Objectives which the enterprise is to achieve and of determining whether or not public enterprise is needed in the first place (i.e. performing the calculus).

The latter is, indeed, crucial, but does not, in and of itself, require a unique statute for each company: the Legislature could make the initial decision and then utilize the C.B.C.A. or equivalent provincial legislation.

The former, too, is critical and may, indeed, justify the use of individual constituent Acts. Unfortunately, as we have already noted, existing empowering statutes tend to couch Objectives in such broad language as to give little guidance as to how the corporation should conduct its affairs. This exacerbates the already high monitoring Costs which pervade the system.

Thus, the best approach may be to utilize individualized constituent Acts which contain far more specific references to the Other Policy Objective(s) which the Crown corporation is to be striving for and to incorporate therein the provisions of the local Business Corporations Act, much as has been done for the Ontario Energy Corporation.[317] The fact that amendments to such a charter will be costlier than in the private sector then becomes perfectly justifiable because the only possible amendment will be to an Other Policy Objective.

The issue of how subsidiaries should be created is somewhat more difficult to analyze. On the one hand, one would, in theory, want to be sure that the calculus is performed by the legislative body each time a new Crown corporation emerges and, further, that the monitoring techniques discussed below apply to them. On the other hand, one may argue that when there are good "business" or legal reasons for creating subsidiaries, why reduce management's flexibility (and further increase Costs) by mandating resort to cumbersome legislative procedures?

We will not, here, attempt fully to resolve this highly controversial issue.[318] We do, however, recommend that the ultimate resolution accomodate an efficient balance of the concepts of accountability and corporate flexibility, as we are viewing them in this paper. At a minimum, subsidiaries created without legislative sanction should be tied to a specific written mandate which constitutes a "subset" of the parent's and should be subject to the same monitoring techniques.

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[17] As well, of course, as a reference to the general monitoring scheme described below which would, likely, be incorporated in umbrella legislation replacing Bill C-24.

[18] It should be noted that perhaps the two most common reasons for creating subsidiaries -- tax planning and corporate acquisitions -- are rarely relevant in the context of Crown corporations. Hence, such activity in the public sector may be suspect *ab initio*.

b) Statutory Immunity:

It is difficult to think of a situation where the Advantages described above can be justified by the need to achieve some Other Policy Objective; perhaps, one could conceive of some amount of pollution being necessary in order to develop a region in a particular manner. Such phenomena are likely so rare that the privilege (which translates to a cost to those who must live in the polluted environment) should be eliminated and trade-offs between two sets of social objectives such as those in the above example should be made on an individual basis, the resulting incremental administrative costs being incurred as necessary.

c) Tort:

No Costs

d) Contract:

No Costs

e) Taxation:

An ample body of literature has developed with respect to whether tax immunities provide the most efficient method of providing subsidies and it will not be canvassed here.

The fact is that the Advantage recognized by provincial Crown corporations in this area relates to the achievement of Other Policy Objectives much in the same manner as does non-payment of dividends: it gives the corporation "extra" retained earnings from which such Objectives can be financed without having to go back to government (and/or into the capital market) for funds and, to the extent that Nationalism is the Objective, permits its achievement with cheaper dollars than the "foreign" competitor could acquire. Indeed, one might argue that it allows for attainment of all Other Policy Objectives with "cheap" dollars, and what is so bad about that?

The answer is complex and involves the following considerations:

1. As suggested by the Wolff Commission with respect to dividends, "profit" from public enterprise should be paid back into Treasury so that it can be used for the many policies which government actively pursues and not just for those of the particular corporation. To use the economic jargon, funds should be paid back to government so that they can be allocated to the project with the highest marginal return, whether or not it is within the mandate of the public enterprise which has produced the revenue. Such reasoning is likely behind the B.C. Committee on Crown Corporation's recommendation to have B. C. Rail pay taxes.[319]

2. If we wish to achieve productive efficiency in the achievement of Other Policy Objectives (and that is, after all, the whole point of this exercise), corporate capital should not be made "artificially cheap" because it may lead managers to allocate marginal dollars to the "wrong" use and may deploy scarce resources away from private sector use.[320]

3. In a similar vein, if capital is not factored in at its true opportunity costs, how will legislators accurately compare the costs of alternative policy instruments and perform the required calculus?

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[19] Committee on Crown Corporations, supra., n., 171, at p. 20.

[20] Hindle, supra., n. 228, at p. 7.

4. During interviews, it was suggested that profit does, in fact, enter into the public manager's Utility function.[321] To the extent that this is the case, there is a real risk that a tax immunity, artificially raising the company's "bottom line", will diminish management's propensity to monitor well because the (artificially-high) "profit" will appear to be quite "satisfactory".[322] Thus, to the extent that we wish to align managerial incentives to the achievement of Other Policy Objectives, tax immunities should be eliminated.

If, in individual cases such as the Nationalism example posed above, it is determined that the Costs of tax immunities are outweighed by the benefits of "cheap money", then a direct appropriation from the Consolidated Revenue Fund can relatively easily (and inexpensively) be made to accomplish the goals now achieved by means of tax exemptions, much in the spirit of the Conservative's 1979 Bill C-27. To any criticism that such approach would cause politicians the added headaches of competitor's complaints regarding such obvious subsidization, I would respond that such competitors already complain about public enterprise's exemption from taxes.

f) Immunity from Criminal Sanctions

The arguments here are analogous to those regarding corporate statutory immunity and I refer the reader to that discussion.

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[21] This issue is key and merits empirical research.

[22] Or, to use Hindle's approach, "satisficing": see Ibid., at p. 3.

g) Labour Relations

Crown corporations subject to public sector employment legislation (including omnibus programs like Equity Employment) recognize both Costs (such as the costs of compliance with such a program) and Advantages (such as insulation from strikes or the freezing of salaries pursuant to B.C.'s Compensation Stabilization Act). These are justifiable in our context only insofar as policy makers have explicitly adverted to the trade-offs involved, much in the same way as we suggested they do in the cases of statutory and criminal immunities.

There is, however, an additional factor to be taken into account here, and that is that legislation like British Columbia's will have direct impact on the pool of talent from which good managers can be chosen and on whether they can be induced to remain in the public enterprise managerial labour market; as we shall see shortly, this will be crucial to the development of a scheme to reduce monitoring Costs.

Accordingly, legislators must, in this context as well, be prepared to remove the hidden Costs of public sector labour legislation and decide on an individual basis whether or not each Crown corporation should be subject to a particular statutory provision; the extra administrative costs which such a scheme would entail should be more than offset by the savings in Hidden Costs.

g) Commercial Immunities

Analysis of the privileges in the commercial law area (such as that provided for under the federal Bankruptcy Act) reveals an analogy to that of to tax immunities: money lent effectively becomes "secured" and, hence, "cheaper" to the corporate lender and the considerations set out above become applicable. Indeed, the argument in favour of removing the privilege is, if anything, all the more cogent here: why should a subset of the population (unsecured creditors) cross-subsidize the achievement of Other Policy Objectives which will, presumably, benefit society as a whole?

h) Immunity from Disclosure Requirements

The exemption from disclosure set out in the Federal Court Act represents an Advantage to the Crown corporation (and a corresponding Cost to society). It might be justifiable in relation to a policy objective such as National Security or to some other which specifically requires that secrecy be maintained. These, however, absent war, are relatively few and far between except, perhaps, in areas such as nuclear research. In such cases, but only in such cases, can the immunity justifiably be maintained.

i) Procedural Privileges

These generate a cross-subsidization of public enterprise in a manner analogous to the preferred creditor status granted under the Bankruptcy Act, here by execution creditors and potential plaintiffs of Crown corporations. Similar reasoning applies.

j) Remedies

The immunity from injunctive relief is similar to several of the others already canvassed and likely represents a holdover from the English view that the Crown, as sovereign, should not be enjoined from acting as it, in its own discretion, considers appropriate. It comprises a subsidy from successful plaintiffs for whom a remedy in damages would not be adequate[323] and should only be maintained if and when it is required to meet some specific Other Policy Objective.

k) The Charter of Rights and Freedoms

The potential Costs here are difficult to quantify; depending on the course of Canadian constitutional law doctrine at this evolving stage, it could prove to be quite large.

It is, however, more than likely that restricting Crown corporate activity in accordance with the civil rights and freedoms set out in the Charter would, if considered by legislators, constitute a valid Other Policy Objective in and of itself, and, hence, would be justified within the terms of reference used in this paper.[324]

l) Monitoring Costs

We move now into our key area of concern, justification of the very high negotiation, information, layering, co-ordination and interpretation Costs illuminated in Chapter III. As we did there, we will examine these in three separate parts: "who", "how" and "what".

(1) The Cost of the Monitors

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[23] The fact that damages are inadequate is true by definition, within the general principles of Equity: if damages were an adequate remedy, then injuctive relief would not be available irrespective of sovereign status.

[24] Needless to say, the Legislature should nonetheless perform the calculus.

Both private and public corporations are potentially subject to the scrutiny of three sets of monitors: shareholders, directors and managers. There are, however, two essential Differences between the two forms of enterprise in this context, the key sources of the identified Costs.

The first is that the shareholder figure in the public sector comprises a multi-partite group. While this is also true in the private sector in the sense that our representative benchmark corporation is widely-held, it can there be said that all of these individuals function as single tier in the hierarchy, irrespective of the fact that they may not agree on particular issues. Not so in the public sector, and the result is layer upon layer of necessary approvals and more and more Costs.

Can these be justified by other Policy Objectives? Surely, to some extent, the answer must be "yes", for without the cheaply, accessible market indicia of profit and share prices, there is no doubt that some extra monitoring will be necessary.

"But need these extra Costs be so large?", we then ask. The response here is "no", they need not, for there is clear duplication of effort and lack of co-ordination involved which can be eliminated without loss to the effectiveness of the monitoring required.

"Why, then, have these not been eliminated, or, at least, reduced?", we continue in the Socratic spirit. The answer is twofold: one, because the legislation has over-structured the accountability regimes (most noticeably in Bill C-24) and, two (and this brings us to the second key Difference from the private sector), because none of the three potential monitors has been given incentives aligned with the ultimate public sector goal of achieving

Other Policy Objectives at minimum cost. Thus, the Costs identified in Chapter III may go to a large extent unchecked.

The solution, I would suggest, is to divert the fundamental orientation of public sector monitoring from its current focus on financial accountability and profit (i.e. from the use of Private Sector Glasses) and towards a confidence generated by safeguards built into the "input" side of the equation.

Firstly, the choice of government as the primary monitor is inappropriate, for it is highly doubtful that with the already hefty responsibilities imposed upon Cabinet Ministers, their concentration on vote maximization and the sheer enormity of the public sector, enough structural or institutional variations could ever be introduced into the existing process to produce maximum results. As Gracey concludes:

> I don't care what legislative framework is in place, what the organizational structures are or might be, or who the personnel are, there are simply too many Crown corporations with too many diverse and complex mandates, many of a huge size, for any government effectively to control or direct.[325]

Rather, I would propose that, in the spirit of the recommendations made by the Lambert Commission in 1979, the appropriate choice of primary monitor is the corporate board of directors, "chosen wisely" and "held accountable for those decisions that its mandate and delegated powers entitle it to make." Such boards should include government representatives as well as experienced businessmen, the former to ensure the necessary liaison between the formulators and the implementors/monitors of Other Policy Objectives by individuals sensitive to the public sector environment, and the latter to ensure that these Objectives are met in the most efficient manner possible. To the potential

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[25] D. Gracey, Speech Notes for I.P.A.C. (Ottawa: unpublished, December, 1984), at p. 5.

criticism (voiced to me by corporate officers in both Quebec and Ontario) that having a Minister on the board would generate a conflict of interest vis-a-vis private sector competitors who fall (for different purposes) within the same Minister's jurisdiction, I would respond:

1. many Crown corporations have no such private sector competitors;
2. Ministers sit on boards in Saskatchewan and British Columbia without apparent conflict;
3. Crown corporations are already the beneficiaries of other privileges; and
4. in any case, the orientation of the Crown corporation is public policy; if the Minister "favours" his Crown over competitors *for reasons* *justified by Other Policy Objectives* *in ways that are not hidden*, isn't that exactly what we want?

Moreover, I would strongly recommend that note be taken of the incentives which motivate these directors to perform well and that the institutional infrastructure be redesigned to utilize them rather than to test them. The central factors here are likely, as we saw above, power, prestige and ease of management. The first and last can surely be bolstered by permitting boards more authority -- "confiding liberally", to paraphrase the Lambert Commission Report. Prestige could, perhaps, be heightened if government were to define Other Policy Objectives well enough that directors' success could be measured in terms of their achievement rather than in the frustrating quest for "profit" in a form of enterprise which was not designed to maximize it.[326]

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[26] Hindle suggests that "systems that allow Crown corporation board mambers/management to be 'promoted' to more prestigious corporations and other forms of personal recognition" be explored; *supra.*, n. 228, at p. 14.

Equivalent incentives should be developed for management, an important secondary monitor in this new infrastructure; as Colin Hindle of Saskatchewan's Crown Management Board concludes, "Steps are necessary to tie the rewards paid to ...corporate management to the performance of the corporation."[327] Remuneration should at least be on par with comparable private sector positions[328] and should include profit-sharing plans wherever possible. The board should have full power to hire and fire. Corporate authority should be delegated to management, much as it is in the private sector; provided that the relevant Other Policy Objectives are well-defined and well-rewarded (via both pay and prestige), there is little reason to suspect that management will not perform. To recall the words of an above-quoted C.E.O., "I wish to ---- that they would just tell me what they want me to do so that I could go ahead and do it for them."

In such a system, extra tiers of government monitors can be eliminated as can regulatory agencies which merely duplicate their monitoring efforts.

(ii) The Costs of the Monitoring Techniques

Chapter III identified a wide array of reporting systems currently used to monitor Crown corporate performance. It also identified their by-products: layering, administrative and co-ordination Costs and disincentives to corporate management.

As above, some level of Costs above and beyond those incurred by the private sector benchmark corporation is, no doubt, justified by the need to

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[27] Ibid.

[28] If anything, they should be higher to reflect the difficulty of management.

monitor performance in the absence of a readily-accessible criterion such as profit; equally of no doubt, the current level of such Costs can be reduced if appropriate systems to reduce them are put into place.

The key here, I would suggest, flows directly from the immediately preceding discussion. If government cannot rely on the motives and abilities of corporate directors and management to produce, then it must couch itself in "lots of paper" in order to protect its investment. To quote Gracey one last time:

> [Bill] C-24 identified the wrong problem and therefore came up with the wrong solution. C-24 is based on the premise that Crown corporations are recalcitrant and untrustworthy. The solution, therefore was to impose layer upon layer of additional controls...[329]

Such behavior is perfectly rational given the existing lack of appropriate managerial incentives and the politician's ultimate accountability to the voter. If, on the other hand, government and the public could rest assured that the institutions have been designed in full cognizance of the motivations underlying managerial behavior and in a manner determined to link these to the achievement of Other Policy Objectives, then some of the paper could happily be dispensed with and Costs could be diminished proportionately.

Some specifics. Annual Reports are warranted but should expressly be required to address how Other Policy Objectives, set out in the previous year's corporate plan (see *infra.*), have been accomplished. Auditors, concerned with financial data, should be selected from the private sector where expertise in commercial-type enterprise is most well-developed; generally accepted accounting and auditing principles should always be employed. Excess layering by Auditors General should be eliminated. Capital budgets should be approved by the responsible Minister as part (but not the focal part) of the corporate plan, *before*

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[29] Gracey, *supra.*, n. 194, at p. 101.

the beginning of each fiscal year; again, specific Other Policy Objectives should be referred to. Operating budgets and quarterly reports should go to the corporate board only, in line with the new orientation to "confide liberally". Borrowing should not require separate approval: it is implicit in the capital budget and the corporate plan and that should suffice.

Finally, and this is likely the most difficult step of all, government must be re-educated in at least two ways: firstly, to distinguish the Crown corporate form from the Department and deal with it as such, and, secondly, to fasten securely its new Public Policy Glasses, to focus not on profit but on efficiency, not on profit but on Other Policy Objectives. This is, perhaps, too idealistic to constitute a "recommendation" as such, but it is fundamental to the creation of an institutional environment which produces the right results.

(iii) The Costs of Specifying Objectives

The Costs incurred in this area are very likely high. Moreover, they have direct impact on the viability of the recommendations just proposed with respect to reducing Costs in the areas of "who" and "how".

At first, one might expect that these Costs would be relatively easy to eliminate: simply do it, specify the Objectives clearly. The problem, of course, is the now-familiar one of political incentives: if Objectives are clearly specified, then they can equally clearly be criticized and "scandalized", at very high cost to the politician. Further, it is likely that given the enormity and intricacy of government bureaucracy, the lag time involved in defining Objectives may be very long and cumbersome.

Within such an environment (which I doubt will change as a result of this paper), I would propose the following: let the corporations do it themselves. That is, as above, have Parliament or the provincial Legislature specify with particularity the broad Policy Objectives which the enterprise should be geared to achieve. Have the corporation then, in an annually-prepared corporate plan, describe these Objectives in terms of specific projects, priorities and trade-offs for Ministerial (i.e. executive) approval: it is far easier for a Minister to say "yes" or "no" to an elucidated, particularized statement than to have her staff prepare it. Moreover, corporate management likely has a comparative advantage over civil servants in preparing such plans and the Minister can still, technically (and that counts in this context), "hide" behind the corporate body if the plan has originated there rather than in her own Ministry.

The corporate plan itself should be shortened to project only for a reasonable interval -- three years, judging by the information gathered in my interviews. It should not be eliminated: it is generally used in the private sector as a key element of the corporate planning process and the evidence obtained in interviews indicates that such plans are used by Crown corporations irrespective of legislative requirements. On the other hand, there seems to be little justification for maintaining the requirement of Cabinet approval of the plans; such process merely adds to the layering problem and, presumably, relies heavily on the responsible Minister's comments in any case. Finally, the Cabinet is very busy and there is little to be gained from requiring an approval which either is not given its fullest attention or is not completed in a timely manner (i.e.the smaller Crowns referred to in Chapter III).

Contrary to some critics, I see no reason why government should not employ the directive to communicate specific policy objectives or changes thereto; indeed, the more such written communication, the better. Further, it has been suggested that flexibility to "change directions" is one variable which has influenced the choice of public enterprise as an instrument of public policy; the closer our new system can be designed to accomodate and, indeed, to utilize, such motivating factors, the better it will function.

Finally, objectives of Crown corporations, government Departments and other instruments of public policy should, in the interests of efficiency, be reassessed and made to overlap only when absolutely necessary to achievement of the Objective in question.

m) The Cost of Capital

We saw above that capital is provided to the Crown corporation far more cheaply than to its private sector counterpart as a result both of lower costs of debt financing and of the lack of pressure to pay dividends to the public holder of corporate equity.

The former, we noted, was a "valid" Advantage in that it reflected the fact that publicly-owned corporations constitute lower risk ventures than do those in the private sector. Thus, comparatively low interest rates are justifiable without reference to Other Policy Objectives and therefore need not be eliminated. However, the additional Costs incurred when government monitors like the Minister of Finance are actively involved in (for example) selecting underwriters, would appear to add nothing substantive to the achievement of Other Policy Objectives and, further, reduces the very flexibility of managers which the scheme proposed here is attempting to expand. As such, these restrictions should be removed.

Non-payment of dividends represents a distinct transfer of wealth to the public enterprise sector of the economy, diminishing the pool of funds from which social, political and economic goals other than those of the corporation in question can be achieved. Moreover, it may have the very negative side-effect of suggesting to management that they have performed satisfactorily when, under the terms of reference employed here, in fact, they have not. Thus, as has been strongly recommended by Saskatchewan's Wolff Commission, government should focus far more on the return it is receiving to its investment in public enterprise and should ensure that corporate management is made aware of the new approach. This is fundamental to planting the correct incentives for manager-monitors.

n) Corporate Authority

This Cost has been referred to several times in the above discussion of developing appropriate incentives for management of Crown enterprise. In short, the Costs which flow from the existing lack of corporate flexibility and control cannot be justified in terms of Other Policy Objectives in a system which has shifted primary monitoring responsibility from government to management; indeed, adequate authority within the corporate structure is one of the cornerstones of such a system, necessary to ensure that correct incentives exist and that the system will operate with lower monitoring Costs than the current one.

Accordingly, provided that corporate Objectives are well documented in empowering legislation, well-interpreted and approved in corporate plans and well-reviewed in Annual Reports and corporate plans of subsequent years, corporate management should be given a wide latitude in determining the course of corporate activity.

o) Other Costs

Several other Differences from private sector activity were documented above.

The first, Costs incurred in customer relations, is justifiable only insofar as direct contact among taxpayer, politician and company president constitutes an Other Policy Objective in and of itself. This is likely not the case. Accordingly, it would seem that customer inquiries should be referred to a "Customer Service Department" just as in the private sector.

Similarly, I can think of no justification for requiring that corporate pricing decisions be made the subject of legislative debate, as is currently the case for companies like I.C.B.C., or that Crown corporations be subject to the administrative procedures employed in government Departments and Ministries. The former is akin to the duplicative efforts of regulators, discussed above, and the latter is merely a symptom of the propensity to view Crown corporations as arms of government instead of simply another type of policy instrument. Both sets of Costs can be eliminated without loss to effective monitoring.

The provision of extra information to government, on the other hand, although it may be viewed by management as an unnecessary burden, would indeed appear to be justifiable by, for example, the Yardstick Objective. If so, then this is a Cost which is validly incurred, as is the Cost related to "Buying Canadian".

VI. Conclusion

The preceding chapters have identified many of the numerous "Hidden Costs" incurred by Canadian Crown corporations and have determined that few are, in fact, warranted in the context of achieving what we have here called Other Policy Objectives. Moreover, the discussion has revealed that none of the players in the public enterprise sector -- government, directors, shareholders or taxpayers -- has an incentive to reduce (let alone eliminate) these Costs.

These deficiencies are crucial not only because of the absolute costs involved, but also because, as Colin Hindle of Saskatchewan's Crown Management Board has pointed out, their existence suggests that, "more efficient public policy instruments may be overlooked"[330], i.e. that the calculus of instrument choice cannot properly be performed.

From this point, the analysis may take one of two directions. One may, as does Hindle, conclude that:

> ...[I]t is essential that government confine 'private' goods producing crown corporations to strictly commercial objectives and that other goals or objectives only be assigned to them on a discrete basis.[331]

As we argued at the outset, such an approach effectively assumes that public enterprise maintains a position in the Canadian economy wholly independent of social, political or economic policy objectives; that is, the use of such Private Enterprise Glasses clouds the fact that the Crown corporation is not merely another form of economic enterprise, but is one alternative instrument of implementing public policy. To assume that Other Policy Objectives

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[30] Hindle, *supra.*, n. 228, at pp. 12-13.

[31] *Ibid.*, at p. 13.

are not integral to this instrument is, therefore, to support the case for privatization.

The alternative -- the approach assumed here -- is[332] to attempt to minimize (ideally, to eliminate) the Hidden Costs and to imbue at least one institutional figure with an incentive structure aligned to the public sector goal of achieving Other Policy Objectives in the most cost-efficient manner. It was to this end that the model in the preceding chapter was sketched.

It is not suggested that the "model" is perfect: indeed, many of its details remain to be delineated. Such detail was not, however, our purpose here. Rather, the goal was to emphasize that a fundamental reorientation of the philosophy guiding the management and accountability of Canadian Crown corporations need be instituted, one which places adequate emphasis on the incorporation of built-in safeguards to a policy instrument operating in an environment in which measurement of output is virtually impossible. With this in mind, I would propose that individuals better-versed than I in the intricacies of Crown corporate structure proceed to develop the appropriate regime.

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[332] On the assumption that privatization is not yet necessary or considered appropriate.

APPENDIX A

Individuals Interviewed

Federal

Mr. P. Marshall, President, Canadian Development Investment Corporation, Toronto, Ontario

Ms. F. Vallee Ouellet, Secretary and Executive Assistant to the Chairman, Air Canada, Montreal, Quebec

Mr. M. Delorme, President, Teleglobe Canada, Montreal, Quebec

Mr. D. Gracey, President, C.G. Management & Communications Inc.

British Columbia

Mr. A. Ree, M.L.A., North Vancouver-Capilano, Victoria, British Columbia

Ms. E. Morrison, F.C.A., Auditor General of the Province of British Columbia, Victoria, British Columbia

Mr. P. Dolezal, President, British Columbia Buildings Corporation, Victoria, British Columbia

Mr. N. Morrison, President, British Columbia Development Corporation, Vancouver, British Columbia

Mr. H.G. Reid, Corporate Secretary and General Counsel, Insurance Corporation of British Columbia, North Vancouver, British Columbia

Mr. G.L. Ritchie, Vice-President - Administration and Secretary, B.C.Rail, North Vancouver, British Columbia

Saskatchewan

Mr. G.K. Wells, Senior Vice President, Finance, Crown Investments Corporation of Saskatchewan, Regina, Saskatchewan

Mr. D.W. Black, President, Saskatchewan Government Insurance, Regina, Saskatchewan

Mr. F. Degenstein, Saskatchewan Telecommunications, Regina, Saskatchewan

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APPENDIX A (cont'd)

Ontario

Ms. G. Gillespie, Senior Policy Advisor, Management Policy Division, The Management Board of Cabinet, Toronto, Ontario

Ms. A. Maurice, Management Board Officer, Management Policy Division, The Management Board of Cabinet, Toronto, Ontario

Mr. L.E. Leonoff, General Counsel & Secretary, Ontario Hydro, Toronto, Ontario

Mr. M. Rowan, President, Ontario Energy Corporation

Quebec

Mr. C. Genest, Executive Vice-president, SOQUEM, Montreal, Quebec

Mr. M. Grignon, Vice-president, Planification generale, Hydro-Quebec, Montreal, Quebec